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VOLUME 9 ISSUE 23

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HIGHER EDUCATION CHOICES

Higher Education Under Fiscal Pressure

Higher education hasn't fared well in the tough fiscal environment of the last several years. By one measure, state appropriations grew at an annual rate of 1.5% in the two years ending in FY 1992. By another measure, the increase in FY 1992 was 2.2%. By any measure, among the large programs of state government -- welfare, higher education, public schools, corrections, and Medicaid -- higher education has been faring least well. Its budget increases have even trailed those of the residual "all other" category.

The situation in many states is worse for higher education than these statistics suggest. The national averages were lifted substantially by a dozen states with either unusually prosperous economies (e.g., Hawaii, Idaho, and Oregon) or major tax increases (e.g., Kentucky, Pennsylvania, and Oklahoma). There were actual cuts in appropriations in 13 states by the two-year measure and in 14 states by the one-year measure. The tables in Issue 22 provide state-by-state detail on higher education's budget problems.

Adjustments To Adverse Fiscal Conditions

Budgets to maintain current services in higher education would cover inflation plus any changes in workload, which for the bulk of higher education activities means full-time equivalent (FTE) enrollment. There is more to public higher education than teaching, but the expensive other activities -- university hospitals, extension services, and sponsored research -- tend to be funded separately. Confronted with state subsidies insufficient to cover enrollment changes and inflation, the public institutions have four broad options for maintaining their operations:

(1) finding other sources of income, with tuition increases having the largest potential followed by increasing alumni and other contributions and selling services such as research, special institutes, and conferences,

(2) reducing their workload by serving fewer students,

(3) increasing their efficiency, broadly defined as the ratio of outputs (e.g., student hours taught) to inputs (e.g. faculty members), and

(4) reducing the cost of their inputs, specifically salaries which are by far the most costly input.

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Raising Tuition To Compensate For Appropriations Cuts

A typical reaction of university administrators confronted with state unwillingness to pay for their product at prices they consider appropriate is to find someone who will pay, rather than change the product. In practice, this means looking at the potentials of tuition increases to maintain spending levels and programs. The math of the trade-off between tuition increases and state appropriations means that relatively small "shortfalls" in state appropriations translate into relatively large tuition increases, particularly in states with traditions of low tuition and high public support. This is illustrated in Table 1.

Table 1: Tuition Increase Needed To Produce Five Percent Per Student Spending Increase

	State Appropriation Increase Percentage					
State Share Of Costs	7.5%	5.0%	2.5%	0%	-2.5%	-5.0%
25%	4%	5%	6%	7%	8%	8%
50%	2	5	8	10	12	15
67%	0	5	10	15	20	25
75%	-2	5	12	20	28	35
85%	-9	5	19	33	48	62

Each entry in Table 1 is the percentage increase in tuition required to give a university or college a 5% increase in spending when tuition is added to the state appropriation increase. How much the tuition increase must be for this to happen depends on: (1) how much the state aid increases, as shown in the column headings and (2) what percentage of instructional costs is paid by the state, as shown in the row headings.

Many states aspire to stable policy in higher education finance, with the ratio between student-financed and state-financed cost constant, such as one-third or one-fourth for the students. To maintain this policy the percentage increases in total spending, tuition, and state support must all be the same. In the table, the target rate of spending increase is 5%, so the 5% column shows the results of a 5% increase in state support. Tuition also needs to rise 5%, regardless of the percentage cost sharing between students and the state.

In states like Vermont and New Hampshire, tuition carries a high percentage of costs, typified by the entries on the top row of the table. In that situation, universities can offset state appropriation decisions by relatively small changes in tuition. But most states are typified by the 67% and 75% state shares shown, with community college tuition sometimes providing 15% or less of costs as shown in the bottom row. In those cases, relatively small changes in state budget decisions cannot be offset by politically feasible tuition increases. For example, to allow a university to increase spending by 5% while the state appropriation is frozen requires a 28% tuition increase in a state that provides for three-fourths of university cost.

Sharp Tuition Increases

On a weighted average basis, tuition at public four-year institutions this year is 12% higher than a year earlier. On an unweighted basis, the increase was 14%. The difference suggests that the greatest increases were found at the smaller institutions. Those increases are massively above the comparable number for private four-year institutions (7%) and even more above inflation (3-5% depending on measure and time period used). Referring back to Table 1, a 12% increase happens to be about what it would take to live with about a 2% increase in state support and still produce about a 5% increase in instructional spending. Table 2 provides a sampling of the tuition increases that were adopted this year.

Table 2: In-State Tuition And Fees, 1991-1992, Selected Institutions

State	School	Total	Increase
Arizona	Arizona State	$1,590	3%
California	Cal. State (Sacramento)	1,048	17
California	U. of Cal. (Berkeley	2,369	17
California	Los Angeles Mission Comm. C.	120	20
Colorado	U. of Colorado (Boulder)	2,308	2
Florida	Florida State U.	1,413	8
Illinois	Malcolm X Comm. C.	985	20
Illinois	U. of Illinois	3,054	7
Michigan	U. of Michigan (Ann Arbor)	3,846	10
Massachusetts	U. of Mass. (Amherst)	5,052	45
Massachusetts	Mass. Bay Comm. C.	1,818	33
New Jersey	Rutgers U. (Camden)	3,670	12
New York	City U. of New York (Brooklyn)	1,955	44
New York	State U. of NY (Albany)	2,285	54
North Carolina	U. of North Carolina (Chapel Hill)	1,213	15
Pennsylvania	Penn State (Univ. Park)	4,402	9
Texas	U. of Texas (Austin)	1,100	8
Virginia	U of Virginia	3,354	13

There are no tuition freezes in the table. Several states, particularly New York, have frozen tuition with pride when circumstances permitted. Most states have some increase every year. Some states achieved the single-digit tuition increases shown in Table 2 through major tax increases. In California, the 17-20% increases reflect the role that restraining state higher education increases played in closing the state's $14 billion budget gap. In New York, with smaller tax increases, and Massachusetts, with none, tuition at major state institutions went up roughly 50%.

Tuition's Impact On Enrollment

While tuition can be an alternative to state appropriations as a source of funding for universities, it is also a price being charged in a marketplace. Raising prices tends to reduce the amount purchased as well as increasing the per-unit revenues to the seller. Higher education is no exception. Consumers have many alternatives to paying tuition at a particular state university including: (1) attending private universities and public institutions in other states, (2) attending less expensive institutions such as community colleges, (3) attending less by taking fewer courses, avoiding summer school, or taking a semester off, and (4) discontinuing attendance at any higher education institution and in the case of potential new students, not starting.

Responses to tuition increases are hard to distinguish from responses to other factors affecting attendance. The responses to the changes at the University of Massachusetts (UMass) have been dramatic, though economic decline in the Northeast has also had an impact. Resident student costs, including tuition, have nearly doubled in four years. Meanwhile applications for admission dropped from about 24,000 in 1988 to about 15,000 this year. The school has sought to maintain enrollment levels by dropping admission standards and increasing recruiting efforts. But it has still seen enrollment drop from a mid-1980s peak of about 19,000 to about 17,000 in 1991.

The Market For Higher Education

Higher education faces a difficult marketing situation. Its primary market, recent high school graduates, is showing declines. One recent study predicts a decline of 3.5% in high school graduates from 1986 to 1995. Within this total, there will be significant differences among ethnic groups with a sharp 52% rise from a small base for Latino students, but a 3% decline for African-American students and a 10.1% decline for "white non-Latino" students. Among this group, there are sizeable increases in fast-growing states like Arizona and Nevada and small increases in many Western states. But changes in this group show the marketing problem of public universities in older parts of the country: Connecticut (-28%), Illinois (-14%), Louisiana (-13%), Massachusetts (-31%), Michigan (-22%), New Jersey (-26%), New York (-23%), North Carolina (-10%), Oklahoma (-11%), Pennsylvania (-18%), and Virginia (-10%).

Confronted with a potentially declining group of customers, public higher education has available all the strategies of any seller. First, existing customers can be encouraged to buy more -- dropping out less, taking five rather than four years to finish, and going to graduate or professional school. Second, market penetration, the percentage of high school graduates who attend college, can be boosted. Third, services can be sold outside the primary market by increased participation by older students, foreign students, continuing education programs, and the like. Fourth, students can be attracted away from private sector institutions.

Enrollment Projections Show Slow Growth, Much Variation

Because of these factors, enrollment trends won't necessarily follow the trend of high school graduations alone. Research Associates of Washington, an outstanding source of 50-state comparisons of higher education data, has developed enrollment projections which appear as Table 3.

Table 3: Percent Change in Public Higher Education Enrollment, FY 1991-1996

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Utah	24.5%	18	Montana	5.5%	34	Alabama	0.0%
2	South Dakota	14.6	19	Texas	4.7	35	Illinois	-0.1
3	New Mexico	14.3	20	Georgia	4.5	36	New Jersey	-0.3
4	Nevada	14.1	21	Missouri	4.2	37	Maine	-0.5
5	Hawaii	13.8	22	Louisiana	3.7	38	North Carolina	-0.5
6	Arizona	13.1	23	Oklahoma	3.6	39	Vermont	-0.7
7	Alaska	12.4		**United States**	**3.3**	40	New York	-0.8
8	Idaho	11.3	24	Mississippi	3.3	41	Tennessee	-0.8
9	California	9.3	25	New Hampshire	3.2	42	Rhode Island	-1.1
10	North Dakota	8.6	26	Iowa	3.0	43	Kentucky	-1.3
11	Washington	8.6	27	Nebraska	2.8	44	Indiana	-2.6
12	Oregon	8.2	28	Maryland	2.6	45	Connecticut	-3.0
13	Colorado	7.6	29	Arkansas	2.5	46	Michigan	-3.3
14	Wyoming	7.6	30	Wisconsin	2.5	47	Ohio	-3.4
15	Minnesota	6.9	31	Virginia	2.1	48	Pennsylvania	-4.0
16	Florida	6.7	32	Delaware	1.9	49	Massachusetts	-4.5
17	Kansas	6.2	33	South Carolina	0.8	50	West Virginia	-6.1

On a national average basis, these numbers are low enough so they don't imply any inherent fiscal problems in financing higher education. The projected 3.3% growth over five years is lower than the expected growth rate of the population and of the number of persons employed. So, for example, the number of workers per university student will increase.

There are three stories reflected in the three columns. States in the last column are expected to see no growth. To fund current services in higher education, they only need to provide for inflation adjustments minus the effect of declining workloads. Their higher education officials will not, of course, see it this way. States in the second column closely resemble the mild growth of the national average. The Western states in the first column face the most serious problems. Utah officials are expecting rapid growth, following nation-leading growth in elementary and secondary schools. California's growth is also expected. There is a plan for massive construction of additional campuses to accommodate the growth, though the plan is currently on hold.

Future enrollments are not independent of price and availability. The projections implicitly assume relatively constant policies regarding the percentage of cost paid by tuition, the growth in cost, and the availability of spaces in public institutions. Sharp tuition increases or more restrictive admissions would cut the enrollment projections. These decisions could also redirect some enrollment -- for example, from four-year residential institutions to community colleges.

Closing Out Students

Nobody's fingerprints are on this decision.

With state appropriations growing less than inflation and formidable barriers to raising tuition enough to make up the difference, something has to give. If asked, legislators would probably speculate that their decisions were being handled by two mechanisms. The first is a reduction in the growth of costs of inputs to the education production process, particularly faculty salaries. The second is an increase in what might be called productivity from each faculty member teaching more students, from elimination of marginal programs, and from trimming of overhead. Critics might characterize the same results as a decline in quality. Adjustments of both types are taking place in many state higher educational systems.

There is another possible adjustment -- simply reducing the number of students served. This makes any given state subsidy a greater amount per student. It thus permits salary increases and avoiding hard decisions such as increasing faculty workload and eliminating programs -- decisions that reduce quality from one perspective and represent increased productivity from another. Because turning eligible students away isn't what most legislators had in mind (and is explicitly prohibited in some states), the action is quiet. But not that quiet, as indicated by a lead article in the Chronicle Of Higher Education (11/13) which discussed it. Administrators of many states aren't talking on the record, so the Chronicle relies on those who can be quoted like Patrick Callan, a former California higher education official quoted at the beginning of this section.

However, the polices are explicit in several states. Minnesota, Oregon, and Wisconsin have adopted formal policies of reducing the size of their major four-year institutions. The subject is being debated in higher education circles in Tennessee, Texas, Utah, and probably other states. In Miami-Dade Community College, the changes are so major they can't escape notice. Given declining per-student support from the State of

Florida, college officials are deliberately reducing enrollment by 3,000 students. The college president explains that the choice was to erode the quality of education or limit access to it.

Access And Student Aid

The recent emphasis on tuition increases to finance public higher education has been deeply disturbing to some policymakers. They see education as the ladder upward for individuals as well as for segments of society, such as the poor. To them public higher education should be about as accessible economically as the public schools.

For decades their positions were reflected in no-tuition policies -- actually low-tuition policies when fees were counted -- in the California system and the City Colleges of New York and low tuition at public institutions in Texas and elsewhere. Sharp percentage increases in these and other schools cause these observers to argue that "access" to higher education is being denied on the basis of income.

Another group is critical of low tuition policies for several separate reasons. First, in traditional economic terms they argue low tuition distorts decisions by encouraging people to take courses who wouldn't do so if they had to pay full social cost. As a result of more student hours, there is also more state spending than economically appropriate. Second, they argue that the policies are driving private institutions out of business or at least making their circumstances difficult. Third, they see the low-tuition policy as a state subsidy for the more affluent, whose children are much more likely to attend higher education institutions.

These critics argue for raising tuition substantially, say doubling it, and providing more extensive student aid for less affluent students. This would mean making the policies of all states less like California and Texas and more like New Hampshire and Vermont.

The rhetoric of tuition increase decisions over the past several years has included a commitment to increased scholarship assistance to offset the tuition increases. But this often means no more than reflecting increased scholarship costs because of the tuition increase, not expanding the pool of those receiving aid. Means-tested federal and state scholarships and loans generally do offset rising tuition for low-income persons. High income persons absorb the higher costs. This leaves the crunch for the middle class, creating concerns that they are being squeezed out of higher education.

Given the experiences of the past two years, many in higher education are convinced that some sort of permanent change in state policies toward higher education has occurred. This is possible, but not obvious. Generally the arguments for higher tuition have *not* been a major factor in state decisions. Instead, the operative decision has been appropriation levels, based on the spending pressures of other programs and the revenue situation. State elected officials haven't been endorsing tuition increases, which they have often sought to constrain, with Virginia a good example. Confronted with better fiscal circumstances, those decisionmakers might well seek to return to the division of cost responsibility between student and state appropriations of the late 1980s.

DEALING WITH THE POOR

The New Attack On Welfare Dependency

This is the first time anyone has had the courage to look at the welfare system and make changes.

This was Governor Schaefer's explanation of his recent proposal for reforming the welfare system in Maryland.

As in other states, the pressures for reform in Maryland are substantial. With a population of a little under five million, the state has almost 78,000 AFDC cases and another 24,000 on the state-funded general assistance rolls. The AFDC caseload has grown 20% in the past year. Welfare costs alone are putting pressure on a state budget that is already out of balance. Higher welfare participation also raises costs in other programs, particularly Medicaid.

The concern over welfare caseloads isn't just fiscal. Welfare is seen as a part of a culture of poverty and dependency that is closely linked to a wide range of social problems including crime, drug abuse, and failure of children in the schools. Politically, high welfare spending is a liability because of welfare's unpopularity. High welfare spending can also make it more difficult to mobilize public, and thus legislative, support for other policies. In Governor Schaefer's case, the policies of interest include raising state taxes and providing substantial support from the rest of the state, particularly affluent suburbs of Washington and Baltimore, to meet the needs of Baltimore.

Maryland's legislature is not the only one that will be considering attempts to deal with welfare dependency. The subject has been a hot topic in Michigan and Wisconsin in the past. The governors of California and Massachusetts, and probably many other states, will likely have proposals as part of their FY 1993 budgets. Legislators in many states will undoubtedly also offer plans even where there is little executive branch interest.

These proposals are getting national attention. Some of it views developments with alarm, as suggested by the title of the Newsweek (12/2) coverage, "A Rough Winter, Running Out Of Money, States Are Testing How Hard They Can Pinch The Poor." Some media coverage lauds what are seen as constructive new ideas, such as Ohio's attempts to get young welfare mothers back into school, as featured in Business Week (October 21).

Responsibility As A Theme

The underlying concept of many of the newer reforms is responsibility. That is, society discharges a responsibility to the welfare recipient only if the welfare recipient acts responsibly relative to society. The concept of a contract between the recipient and the state is sometimes used.

The definition of responsible conduct varies from state to state. The Maryland proposal is to cut the AFDC grant by 30%. The recipients earn the full grant back by meeting state standards for: (1) keeping their children in school, (2) making sure their children get preventive health care, and (3) paying their rent. The incentive to keep children is school is part of what Wisconsin calls "learnfare." An incentive to work, or at least seek work and prepare for it, is now a part of all state AFDC programs.

The plans involving placing special requirements on AFDC recipients generally require waivers from the federal government. Changes in general assistance, which is 100% state and local money, do not.

From Welfare To Jobs, Maybe

There is broad consensus that work is the solution to welfare dependency.

Non-incumbent candidates for state and federal office are constantly offering this solution. When they become incumbents, they are constantly implementing it. The result is a constant series of announcements leading to headlines like, "State Planning A Workfare Program" which appeared in the Boston Globe recently (11/6).

These programs are not new. Federal legislation has required states to operate some sort of welfare-to-work program since 1968. The latest version is required by the Family Support Act of 1988, then known as federal welfare reform legislation. It creates the JOBS program, which replaces other programs like WIN, WIN-Demonstration, Job Search, Community Work Experience, and Work Supplementation. In Massachusetts, specific programs, each with a catchy acronym or program title, were adopted in the early Dukakis days of the 1970s, under Governor King, and under the second Dukakis Administration where the program, called ET, received widespread national publicity. The new program will probably have a catchy title also, Mass Jobs. For all of the new emphases, the federal spending for work-to-welfare programs, adjusted for inflation, is less than in the peak year of FY 1974.

While hopes are high for these programs, dramatic results aren't being assumed in federal projections of AFDC costs. As a recent General Accounting Office assessment put it, "However, service and funding shortages and poor economic conditions could decrease states' abilities to operate JOBS and slow their progress." The barriers to success as the programs are currently constituted are formidable:

- It is not economically advantageous for current welfare recipients to work at jobs likely to be available. Forgetting subsidized transition periods, the worker incurs transportation, child care, clothing costs, and taxes. To get what is left after these costs, the former welfare recipient forgoes cash assistance, Food Stamps, Medicaid, and other income-tested programs. In the proposed Massachusetts program, this is reflected in a cutoff point of about $7 an hour, with a welfare recipient allowed to turn down work not paying that much -- a level about twice the minimum wage. An analysis of the California GAIN program by the legislative fiscal staff suggests the breakeven point for a welfare family of three is a job paying $1,400 per month or about $8 an hour.
- Particularly in current economic circumstances, it isn't easy to find a job. Doing so is harder for those without substantial work histories and education.
- Evaluations of past work-to-welfare programs suggest they are only close to breakeven in long term assessment of state government costs and savings. This doesn't mean they aren't worthwhile, but they don't offer the dramatic payoffs that would encourage their funding. This is probably why many states didn't use all the federal money available to them in FY 1991.
- Even if they offer to break even in the long run, the programs involve heavy front-end outlays for training and placement in return for a stream of future savings from avoiding welfare payments -- a cost profile similar to buying new cars to avoid maintenance costs of old cars. In times of fiscal stringency, programs with this cost profile are some of the earliest to be cut in state austerity moves.

Cutting Payment Levels

> *We pay 3 1/2 times the welfare grant that Texas does, about double what Arizona does. I think, in part, we have been an attractive destination for people who were out of work and on welfare in other states.*

Paying less per recipient has always been a potential money-saving adjustment in AFDC and general assistance programs. Conversely, concern over low payment levels relative to living costs and payments of other states has always produced pressures to raise payments.

Over the past two decades, states have been increasing their cash payment levels less than inflation, making the cash payment levels lower in constant dollars. The impact has been offset in part by growing Food Stamp benefits and other programs, such as low-income heating assistance.

Providing no increase in the AFDC grant is a standard response to state fiscal problems, particularly when state employees are doing without pay increases. California cut its cash assistance level as part of budget decisions earlier this year. The payment level may again be under attack, as indicated by the comment of Governor Wilson, quoted above, in discussing ways to deal with the new shortfall that has appeared in the budget.

The extreme disparities in payment levels are shown for selected states in Table 4. Alaska's level is twice the U.S. median payment of $367 a month for a three-person household. Benefits in some states are less than half this amount.

Table 4: AFDC Monthly Cash Payment For Family Of Three, January 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Alaska	$891	8	Massachusetts	$539	32	Ohio	$334
2	California	694	9	Minnesota	532	36	Florida	294
3	Connecticut	680	11	Michigan	525	41	North Carolina	272
4	Vermont	679	12	Wisconsin	517	48	Texas	184
5	Hawaii	632	18	Pennsylvania	421	49	Alabama	124
6	New York	577	25	Illinois	367	50	Mississippi	120

Reforming General Assistance

The AFDC program handles cash assistance for families with children in the household. The federal SSI program deals with cases involving: (1) age over 65, (2) disability, and (3) blindness. Many persons without income don't fit into any of these categories. These individuals receive general assistance, which involves no federal participation in cost or regulation. Some of these programs are state administered; some are administered by local governments. Benefit levels and eligibility standards vary substantially. In most descriptions, a few states are said not to have any such program.

General assistance is now under attack. The move is most extensive in Michigan, where large numbers of recipients were recently cut off entirely from state assistance. The action has generated national publicity that is likely to lead to similar moves in other states in the budget cutting environment predicted for early next year. There are somewhat similar restrictions on the program now going into effect in other states, such as Ohio.

Measuring Poverty In Individual States

The Census Bureau has recently released estimates of poverty levels by state, subject to caveats appearing in the Technical Notes at the end of this issue. The data appear in Table 5.

Table 5: Percent of Persons In Poverty, Average 1988-1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Connecticut	4.3%	18	Virginia	10.9%	34	New York	13.4%
2	New Hampshire	6.9	19	Alaska	11.0	35	Florida	13.5
3	New Jersey	7.9	20	Hawaii	11.1	36	South Dakota	13.6
4	Rhode Island	8.0	21	Nebraska	11.1	37	Arizona	14.0
5	Delaware	8.5	22	Ohio	11.5	38	Georgia	14.9
6	Wisconsin	8.5	23	Minnesota	11.6	39	Montana	15.5
7	Utah	8.7	24	Maine	12.2	40	Oklahoma	15.9
8	Vermont	9.0	25	Indiana	12.3	41	South Carolina	16.2
9	Washington	9.1	26	North Dakota	12.5	42	Kentucky	17.0
10	Massachusetts	9.3	27	North Carolina	12.6	43	Texas	17.0
11	Maryland	9.6	28	Colorado	12.8	44	West Virginia	17.2
12	Kansas	9.7	29	Missouri	12.9	45	Tennessee	17.8
13	Nevada	9.7	30	Illinois	13.0	46	Alabama	19.1
14	Iowa	10.0		**United States**	**13.1**	47	Arkansas	19.8
15	Oregon	10.3	31	California	13.3	48	New Mexico	21.1
16	Wyoming	10.5	32	Idaho	13.3	49	Louisiana	23.2
17	Pennsylvania	10.6	33	Michigan	13.2	50	Mississippi	25.0

Poverty And Welfare Participation

For complex reasons not fully understood, the participation rate in means-tested programs is substantially below eligibility. The list of reasons includes a mix of pride, lack of understanding, fear of having to deal with caseworkers, and potential statistical errors in estimating the population that might be eligible. There are also some conceptual differences between poverty, measured by income, and welfare eligibility, measured by assets and income. Welfare eligibility also varies considerably among the states. While unable to explain the numbers, **Reports** presents a comparison of selected states in Table 6 (next page). It compares the poverty rate, the participation rate for the nationally uniform Food Stamp program, and the participation rate in AFDC. The rankings assume more participation is deserving of a higher rank.

The expected relationship is that shown for the U.S. There is a substantial fall off from poverty status to participation in Food Stamps and a further substantial fall off from

Food Stamp participation to AFDC participation. Some indication of the generosity of the California payment levels and eligibility standard is suggested by nearly identical participation rates in AFDC and Food Stamps. There are many persons eligible for Food Stamps who can't be on AFDC because there are no children in the household. So, in California, the data suggest there are likely many persons who either cannot or choose not to apply for Food Stamps but do receive AFDC.

Table 6: Percentage Of Population In Poverty and Receiving Food Stamps And AFDC And Rankings Among States In Percentages, Selected States, Various Years

	Ranks			Percentage Participating In:		
State	Poverty	Stamps	AFDC	Poverty	Stamps	AFDC
United States				**13.1%**	**8.1%**	**4.6%**
Mississippi	1	2	2	25.0%	19.4%	6.9%
Louisiana	2	3	3	23.2	17.2	6.7
New Mexico	3	8	19	21.1	10.4	4.1
Arkansas	4	9	40	19.8	10.0	3.0
West Virginia	7	1	5	17.2	20.2	6.1
New York	17	14	8	13.4	8.6	5.5
Michigan	18	11	1	13.2	9.9	7.0
California	20	26	4	13.3	6.5	6.4

Michigan has a larger spread between Food Stamp and AFDC participation. But it leads the nation in AFDC participation despite trailing 10 states in Food Stamps and 17 states in poverty rates. The numbers also suggest there are more recipients of Food Stamps in West Virginia than there are poor people.

Causes Of Growing Caseloads

The large gap between the poverty rate and participation in Food Stamps and AFDC indicates the potential for substantial further growth in those programs. Factors that influence participation may be as important in causing growth as underlying economic factors like poverty and unemployment. Indeed, a recent survey by the American Public Welfare Association asked state officials to rank reasons for caseload growth. Out of 44 states responding, "the worsening economy" was ranked as most important by 25. But officials of 18 listed "enhanced Medicaid benefits program" as most important and another nine listed the Medicaid factor as second most important in causing caseload growth.

The report explains, "As states increase outreach efforts to reach these new populations {women and children newly covered by federal mandate} and determine eligibility for Medicaid services, states are also finding that many are eligible for Food Stamps and AFDC." In simple terms, caseworkers are seeking out expectant mothers and mothers with young children to bring them the preventive health services now covered under Medicaid. In the process, they are finding people who qualify for cash assistance.

Welfare, Medicaid, and Social Priorities

> *The irony here is powerful: because Congress mandated better health care for the poor, at least some Illinois residents will lose welfare benefits.*

With this comment, Newsweek (12/2) bought the argument that federal Medicaid mandates are hurting the poor. The argument is pretty clearly true, though hard to prove except by anecdotal evidence. Medicaid mandates have made state budgets tighter than they would otherwise be. The result has been some combination of taxes higher than they would otherwise have been and allocations for other state programs -- including education as well as welfare -- lower than they would otherwise be.

In state budgets, spending on health care for the poor exceeds by far spending on cash assistance for the poor. In the budgets approved for FY 1992, total Medicaid appropriations were $35.9 billion while AFDC appropriations were $8.1 billion, making Medicaid over four times as expensive. The increase from FY 1991 to FY 1992 was $96 million for AFDC and $6,423 million for Medicaid. Put another way, 98% of the new spending in these programs for the poor is going to health care.

FISCAL PROBLEMS CONTINUE

Introduction

With recession showing no signs of abating, the fiscal circumstances of just about every state are looking worse. Compared with the outlook when budgets were adopted earlier this year, there appears to be: (1) less likelihood that the FY 1992 budget is balanced and (2) more likelihood that the FY 1993 budget to be adopted next year will need major spending cuts and/or tax increases to be balanced. The state-by-state details appear in State Budget & Tax News.

Circumstances are so common among the states that materials from one can almost be lifted verbatim for use in another. To illustrate this, the next three sections quote extensively from recent reports in three different states. The quotations are changed by minor editing. Local references (e.g., Jefferson City) have been replaced with generic citations (e.g., state capitol) and local numbers replaced with citations to "amount." On the theory that which state is which doesn't matter, the states aren't named here. On the theory that readers may not buy that theory, they are listed in Technical Notes at the end of the issue.

Sample Report One: Watchdog Group

The first example of appraisals.of state fiscal condition is a summary assessment by an outside watchdog group like an expenditure council, taxpayers' federation, or state chamber of commerce.

> *Earlier this year, the* (governor) *administration was able to close an over $* (amount) *income-outgo gap through a combination of actions, including selected workforce reductions, the deferral of certain payments, and other one-time financing mechanisms as well as* (if applicable) *increasing the tax rates on* (specify). *Even with the new revenues generated, the Governor and lawmakers could only adopt an austerity budget providing* (specify) *percent growth in FY 1992 state spending. Furthermore, as we noted when that fiscal plan was enacted in June, the FY 1992 state budget left "no room for the unexpected," with all of the state's anticipated resources being committed.*
>
> *Unfortunately, the national recession, the* (specify local emergency like floods, bank failure, collapse of local finances) *and the state's high unemployment levels have not only continued to depress state tax collections but also appear to have contributed to mounting welfare and medical assistance caseloads. For example, when the* (state's revenue estimators) *met to review actual collections and the latest economic forecast, they lowered their consensus general revenue estimate for FY 1992 by another $* (amount). *In combination with their earlier revision this summer, the estimators are now expecting only $* (amount) *in receipts in the current fiscal year -- a projected shortfall of $* (amount) *compared to the $ (amount) estimate upon which the FY 1992 budget was based.*
>
> *On the expenditure side of the fiscal equation, caseloads for AFDC, general assistance, and Medicaid are now projected to increase, adding to state expenditures at the same time revenues are falling. The budget imbalance may grow larger if there is a need for increased medical assistance, welfare payments, and other possible deficiency spending items.*
>
> *Of course, the state reportedly received a 'windfall" earlier this year in a federal Medicaid reimbursement for its disproportionate share of low-income patients in public hospitals* (rephrase to reflect exact bootstrap financing plan, if any). *These monies were used to* (reimburse for mechanisms used to balance FY 1991 budget, if applicable) *as well as to establish a reserve to cushion the state against any FY 1992 imbalance.*
>
> *This does not belie the fact that (state) not only faces a significant income-outgo gap in the current fiscal year, but also a potential deficit of over $* (amount) *in FY 1993. Previous fiscal imbalances were closed by increasing taxes, austerity budgets, and one-time financial plans. As the Governor and legislature consider options for dealing with the current difficulties, they should avoid the temptation to turn to "quick fixes" and instead take decisive steps to lose this structural gap by reassessing the role of state government in the 1990s. Now is the time for reform.*

Sample Report Two: Group Interested In Spending

The second example is from a group interested in social service spending.

> *The state's budget, balanced with no room for error, is quickly moving out of balance as a result of revenues already coming in below estimates, general assistance, adult corrections and Medicaid spending exceeding appropriations and several unfunded liabilities. The way things are going, the deficit could build to $* (amount) *this fiscal year.*
>
> *A deficit of this size cannot be made up by budget cuts alone in a budget which is as tight as the one enacted for this* (year, biennium). *There is only $* (amount) *left in the state's "Rainy Day" Fund. Temporary tax increases would be a political "cop-out" which fails to recognize that the state's fiscal problems are systemic -- they are not temporary. They result from the fact that service needs are greater than existing revenue sources will provide. They result from the accumulation of four years when the state drew down its reserves and used other one-time revenue sources.*

Sample Report Three: Major Newspaper

The last example of how fiscal assessments from one state are applicable to many other states comes from a newspaper account.

> *(State Capitol), (Date)-- Governor* (name)*'s budget office said today that the gap in the coming state budget may rise to $* (amount), *double its previous estimate, or more than* (number) *percent of the total projected budget.*
>
> *Officials said they based the new figure on projections that the state and national economies would take still another turn for the worse, depressing tax collections and increasing spending on social services.*
>
> *The governor seized on the worsening state budget problems as all the greater reason for legislative leaders to agree on a multiyear budget that he said could begin to attack the deficit problems now rather than when FY 1993 is to begin. In the current fiscal year, the state is already facing a gap of at least $* (amount), *and the governor has warned this could go even higher.*

What Is To Be Done?

> *To put it in simplest terms, the four leaders reported to me that they could not find in their individual caucuses any enthusiasm for a tax increase. So to cut through it, what we are confronted with is the necessity to look at very painful spending cuts.*

This was Governor Wilson's conclusion after meeting with California legislative leaders of both parties in November. The result is indicative of sentiment around the nation that the current shortfalls should be handled by spending cuts rather than tax increases.

A determination in the fall to avoid tax increases the following year doesn't mean there won't be tax increases. Similar determination in 1982, when recession was hurting state finances, was followed by many increases in 1983. State Budget & Tax News (Issue 21) lists 11 states with 30% of the population as places to look for increases in 1992. Even in those states, there is little discussion of tax hikes except in states where increases were discussed this year but not enacted -- Alabama, Colorado, Florida, Kansas, and Tennessee.

COMPARING PROGRESSIVITY OF TAX SYSTEMS

The progressivity of state/local tax systems can be compared by many measures. However, a relatively simple measure like that shown in Table 7 illustrates the differences.

Table 7: Index of Progressivity for the Largest City in Each State, 1990
Taxes at Income of $25,000/Taxes at Income of $100,000

Rank	City	Index	Rank	City	Index
1	Minneapolis, Minnesota	0.43	26	Milwaukee, Wisconsin	0.91
2	**Los Angeles, California**	**0.62**	**27**	**Portland, Oregon**	**0.91**
3	Boise City, Idaho	0.69	28	Atlanta, Georgia	0.91
4	**New Orleans, Louisiana**	**0.69**	**29**	**Louisville, Kentucky**	**0.91**
5	Portland, Maine	0.70	30	Jacksonville, Florida	0.93
6	**New York City, New York**	**0.73**	**31**	**Des Moines, Iowa**	**0.93**
7	Wilmington, Delaware	0.73	32	Newark, New Jersey	0.94
8	**Billings, Montana**	**0.76**	**33**	**Fargo, North Dakota**	**0.96**
9	Charleston, West Virginia	0.78	34	Denver, Colorado	0.96
10	**Little Rock, Arkansas**	**0.79**	**35**	**Phoenix, Arizona**	**0.96**
11	Columbia, South Carolina	0.80	36	Baltimore, Maryland	0.96
12	**Honolulu, Hawaii**	**0.81**	**37**	**Chicago, Illinois**	**1.00**
13	Oklahoma City, Oklahoma	0.81	38	Bridgeport, Connecticut	1.02
14	**Jackson, Mississippi**	**0.81**	**39**	**Omaha, Nebraska**	**1.03**
15	Boston, Massachusetts	0.81	40	Indianapolis, Indiana	1.05
16	**Norfolk, Virginia**	**0.83**	**41**	**Manchester, New Hampshire**	**1.07**
17	Alburquerque, New Mexico	0.83	42	Birmingham, Alabama	1.10
18	**Wichita, Kansas**	**0.83**	**43**	**Philadelphia, Pennsylvania**	**1.10**
19	Burlington, Vermont	0.84	44	Casper, Wyoming	1.11
20	**Charlotte, North Carolina**	**0.85**	**45**	**Seattle, Washington**	**1.12**
21	Cleveland, Ohio	0.87	46	Anchorage, Alaska	1.14
22	**Detroit, Michigan**	**0.89**	**47**	**Houston, Texas**	**1.15**
23	Providence, Rhode Island	0.89	48	Las Vegas, Nevada	1.15
24	**Salt Lake City, Utah**	**0.89**	**49**	**Sioux Falls, South Dakota**	**1.21**
25	St. Louis, Missouri	0.90	50	Memphis, Tennessee	1.22

The table expresses the relationship between tax rates as a percentage of income in each city for families with incomes of $25,000 and $100,000. If taxes were proportional to income, both income levels would pay the same percentage, say 9%, though the higher income household would pay more tax. In the table, the proportional tax situation would show a progressivity index of 1.0.

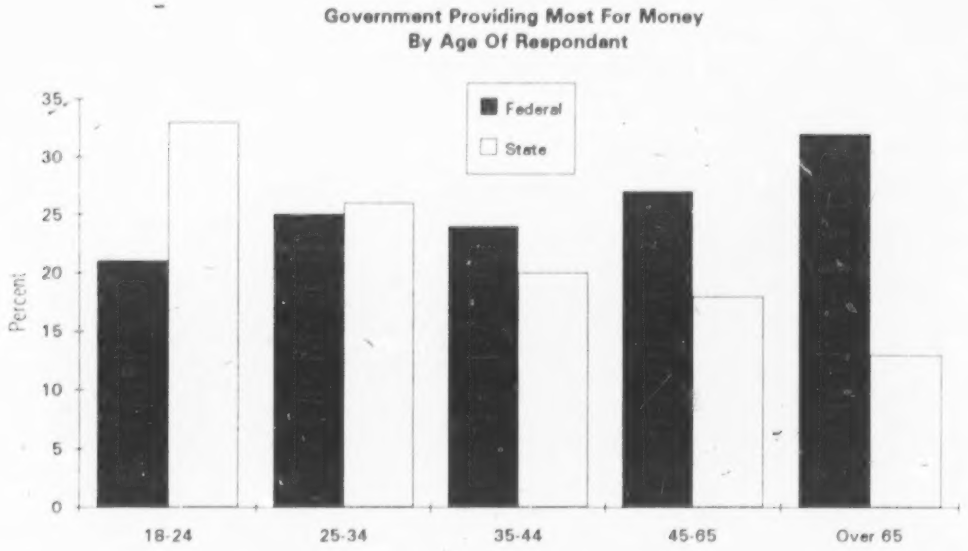
Thirteen states have regressive tax systems by this measure as shown by values over 1.0, meaning that lower income families pay a higher proportion of their incomes in taxes. This is a smaller number of regressive tax systems that many studies of state tax systems show because use of an extraordinarily high income of $100,000 brings out the steepest rate in graduated state income taxes. The states shown as regressive are mostly states without income taxes.

WHICH GOVERNMENT HELPS THE MOST?

The Advisory Commission on Intergovernmental Relation's annual public opinion poll (Changing Public Attitudes On Government And Taxes: 1991) is the standard source of information on which tax is least favored (property), which government spends money most wisely (local), and other public finance topics. The detailed report breaks down the responses by categories of the people surveyed including sex, race, age, education, employment status and occupation, household size, and region. Most of these breakdowns aren't particularly interesting because they show only minor differences or obvious ones, such as the finding that the more education people have the more likely they are to know that states have their own constitutions.

The exception is how differently people of different ages answered the question, "From which level of government do you feel you get the most for your money: Federal, State, or Local?" Overall, local government won with 31%, the federal government placed second with 26%, and state government with 22% tied with "Don't Know/No Answer." Age affected the responses as shown in the chart on the following page. Appreciation of state governments is greatest among younger age groups and drops significantly with increasing age. The fall-off of support extends to local government as well. Support for local government is highest in the 35-44 group and falls off to 28% among those over 65. The federal situation is reversed, with support highest among older persons.

The differences make considerable sense. The federal government isn't a particularly good deal for younger adults who pay the steep Social Security payroll tax as well as the income tax and don't see many benefits. State governments provide universities and community colleges and roads for the younger set as well as paying half of pubic school costs for their children. By age 65, these state contributions are less important, Social Security and Medicare are extremely important, and the federal tax burden drops on retirement.



There is bad news here for support of state and local taxes. The older people get, the less likely they are to think they get their money's worth from those taxes. People are, on average, getting older. Furthermore, the tendency to go to the polls also increases with age.

THE STATE POLICY BOOKSHELF

Two new books have appeared with piles of data on government policy and finances -- enough to provide a basis for a brief quiz.

New States In Profile

The second 1991 edition of States In Profile should reach the 80% of readers who have full service **Reports** subscriptions about the time this issue does. *(To purchase additional copies, call the subscription office listed on p. 2 of this issue.)* Besides providing a deskbook for interstate comparisons, the book, if memorized, can make readers expert enough to get perfect scores on the test below (answers on page 24).

(1) Name three of the six states that experienced the most population growth between 1980 and 1990.

(2) The median age in Florida is nearly 37, well above the national average. Name any one of the next highest six states.

(3) Manufacturing accounts for more than 24% of jobs in five states. Name three.

(4) In the typical state, do state governments raise more money than local governments?

(5) State government debt per capita is now: (a) over $10,000, (b) about $5,000, (c) about $1,000, or (d) well under $1,000.

(6) State and local taxes take about 11.6% of people's income, but the take is over 15% in Alaska (where oil companies pay most of it) and nearly 16% in what state?

(7) Five states qualify as being among the 10 lowest tax states whether low state and local taxes are measured per capita or in relation to personal income. Name two of them.

(8) Federal grants to state and local government average just over $500 per capita. Only two states get over twice the national average. They are states with what characteristic: (1) the least revenue-raising capacity, (2) the largest percentage of poor people, (3) the largest percentage of people living in large cities, or (4) the most revenue raising capacity?

(9) Spending per pupil in public school is at least 30% above the national average in five states and at least 30% below in six. Name three states in either group.

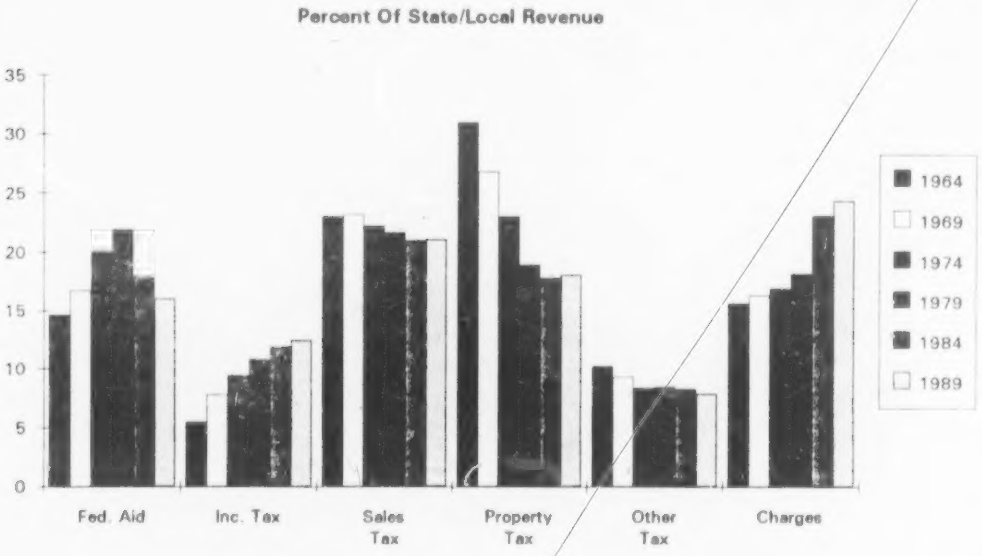
(10) States differ by region in strategies for their "flagship" universities. One region has high spending financed by high tuition, while others have more moderate spending and tuition, and still others maintain relatively high spending with low tuition. Name one region linked with a strategy.

(11) Nationwide, one child in a hundred dies soon after birth but the rate is 20% higher in five states. Name two.

Bonus Question For World Class Trivia Buffs: One state spends only 2.8% of state and local budgets for law enforcement, lowest in the nation and less than half the national average. Its violent crime rate is only one-tenth the national average. Name the state.

New Significant Features

The annual two volume set Significant Features Of Fiscal Federalism belongs on the bookshelves of most readers of **Reports**. The second 1991 volume, with most of the statistical data, 330 pages of it, appeared recently. Its greatest strength is the large collections of historical data, providing national summaries of trends in taxes and spending for all three levels of government. An example is the shift in where state and local governments get their money as shown by the chart.



The chart shows differing patterns for the major revenue sources over the past 25 years. User charges and individual income taxes have played growing roles in financing state and local government while federal aid peaked and receded. Property taxes consistently declined but have shown some signs of revival.

TECHNICAL NOTES

Higher Education: Table 1 was calculated by **Reports** and can easily be calculated by readers for any percentage gain in per-student spending deemed of interest. Table 2 is from the College Board as reprinted in the Chronicle Of Higher Education (10/23). Research Associates of Washington (2605 Klingle Road, NW, Washington, DC 20008) publishes state-by-state statistics on higher education in State Profiles: Financing Public Higher Education 1978 to 1991. It has other publications also oriented to state-by-state comparisons in higher education such as Higher Education Revenues & Expenditures: A Study of Institutional Costs.

Academics being prolific writers, there is no shortage of book-length treatments of higher education finance and management issues generally, and student access issues in particular. For a recent treatment of the affordability arguments that is rich in historical statistics see Michael McPherson (Williams College) and Morton Schapiro (U. of Southern California), Keeping College Affordable (Brookings, 1991).

Dealing With The Poor: The poverty percentages are from the Census Bureau's Poverty In The United States: 1990, a volume that provides considerable demographic detail on the poor. These data are not available by state except for the total poverty population. Census warns against state-by-state rankings but itself calculates year-to-year changes, which is statistically even more adventuresome. These concerns are less serious than undercount concerns. If Census missed 5 million Americas in the 1990 Census, then none of the poverty rates are accurate.

The comparison of AFDC and Food Stamp participation involves slightly differing years. The poverty information is that in Table 5 ranked from high poverty to low. The other participation rates are from the new States In Profile, Table H-4 and H-10. The assessment of JOBS activities from the General Accounting Office (Washington, DC 20548) is Welfare To Work: States Begin JOBS, But Fiscal And Other Problems May Impede Their Progress. The survey of reasons for caseload growth comes from the American Public Welfare Association (810 First St., NE, Washington, DC 20002). The comparison of budgets for AFDC and Medicaid comes from NCSL's State Budget And Tax Actions: 1991.

State Finances: The first sample is from the Rhode Island Public Expenditure Council's RIPEC Budget Watch (11/7). The second is from the Cleveland-based Federation For Community Planning's The Budget $cene In Ohio (November). The third is from reporting on New York State in the New York Times (11/20).

Progressivity: The District of Columbia Department of Finance And Revenue (Office of Economic and Tax Policy, 300 Indiana Ave., NW, Washington, DC 20001) prepares an annual comparison of burdens of major taxes on residents of the largest city in each state. The volume, Tax Rates And Tax Burdens In The District Of Columbia: A Nationwide Comparison, is useful in comparing individual taxes from state to state as well as in calculating progressivity.

Bookshelf: Significant Features is published by the Advisory Commission on Intergovernmental Relations (800 K St., Suite 450, Washington, DC 20575). The chart was developed by **Reports** from one of the many historical tables.

Answers To Quiz

(1) Fastest growing states in order have been Nevada, Alaska, Arizona, Florida, California, and New Hampshire.

(2) Other states with high median ages are in the Northeast (Connecticut, Pennsylvania, New Jersey, New York, Rhode Island, and Massachusetts). Other retirement destinations like Arizona, Nevada, and Texas are below the national average.

(3) The heavy manufacturing states are North Carolina, followed by Tennessee, Michigan, Indiana, and New Hampshire.

(4) In most states, the state raises just under half the money and local government just over half but Hawaii raises 71% while New York and New Hampshire are under 40%.

(5) State debt averages about $1,300 per capita with 20 states below $1,000. Twenty states could pay all their debt with half a year of their revenues and 40 states could make full payment with less than one year's revenues.

(6) New York taxes are second highest by this measure followed by Wyoming, Hawaii, Maine, and Minnesota.

(7) By either measure, Alabama, Arkansas, Mississippi, South Dakota, and Tennessee are low tax states. By the representative tax system (Table D-15 in Profiles), the Southern states rise in rankings compared to the other measures with New Hampshire getting the honors (stigma) for the lowest tax state, followed by Nevada, Florida, and Tennessee. New York is unambiguously the highest tax state by the RTS measure.

(8) The top states in federal grants per capita, Alaska and Wyoming, are the top states in revenue-raising ability.

(9) High spending states are New Jersey, New York, Connecticut, Alaska, and Rhode Island. Lowest spenders are Utah (56% of the national average), Idaho, Mississippi, Arkansas, South Dakota, and Alabama.

(10) High tuition-high spending per student strategies predominate in the Northeast where state support per pupil is the lowest. Midwestern states pursue this strategy a little less vigorously. States West of the Mississippi, with exceptions, follow the opposite strategy.

(11) Infant mortality is regional with the highest rates in Georgia, North Carolina, Mississippi, South Carolina, and Alabama.

Bonus Question: The combination of low law enforcement spending and low crime rates is found in North Dakota. Good guesses were Montana and Vermont. The trick is to export both criminals and victims, as crimes are reported by place of occurrence. This question is so hard that when tried on a panel of three experts, all three missed it and the **Reports** editor couldn't correctly remember the right answer.

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VOLUME 9 ISSUE 24

SPR

STATE POLICY REPORTS

IN THIS ISSUE

Recession is affecting some states much more than others as indicated by the latest Index of State Economic Momentum. With few exceptions, Western states are outperforming Eastern states. California has been falling off the top of some economic indicators while new stars like Nebraska and Utah are appearing.

- State Economic Performance p. 2

While some states are doing better than others, the falling national economic tide is lowering all boats. In preparing their new budgets, state officials will have to guess when economic recovery will begin. In some states, they are searching for a way state government can act to hasten recovery.

- The Economy And State Finances p. 11

Congress completed its work in 1991 with some boosts for state finances. The federal tax changes now being discussed would also affect state tax systems.

- Federal Impacts On State Finances p. 14

Public opinion polls show widespread approval of spending for particular programs and widespread disapproval of taxes.

- Public Opinion p. 18

Some states with the highest personal incomes have lost the most, but still have massive advantages over other states by many measures. Nevada is tops in one measure of in-migration and is predicted to be tops in drawing retirees.

- Comparing Affluence Among The States p. 20

Technical notes detail sources and calculations.

- Technical Notes p. 24

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STATE ECONOMIC PERFORMANCE

Introduction

Governor announces recent job gains, says state development strategy working.

Study criticizes state's business climate, says development lagging.

Legislative leader predicts more budget cuts, maybe tax increases too, says problem is national economy.

These are examples of statements that imply something about how a state relates to other states. The statements beg for some measure of state performance relative to the nation and other states. For example, gaining 20,000 jobs isn't impressive if it's a lower percentage gain than the nation and 30 other states. Blaming budget cuts on national economic stagnation makes little sense if a state is far outperforming the nation.

How well are individual state economies performing? While there is no perfect way to answer this question with one statistic, the Index of State Economic Momentum is as close as anyone has come. The Index, which appears quarterly in **Reports,** measures a state's performance relative to the national average.

The Index Of State Economic Momentum

The Index is based on the most recent known changes in: (1) employment, (2) personal income, and (3) population. These changes for each state are related to the national average change for that measure. The differences are averaged for each state with the result expressed as the index number. The national index is 0.00, as the national average has no deviations from the national average.

Minor differences among states in economic statistics shouldn't be taken seriously. The population estimates are from a Census that may have overlooked five million people. The job data double-count some employees. The personal income statistics exclude the underground economy. But larger differences among states are significant, as evidenced by such indicators as how much budget trouble different states are experiencing.

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Winners And Losers

The latest Index appears as Table 1. The table shows an unusual distribution of states. The top 13 ranks are held by less populous states in the West. Most of the large industrial states are just above or below the national average. The bottom ranks are held by the New England states. Of the top 25 states, 23 are on, or West of, the Mississippi River. The exceptions are Florida, ranked 22nd, and Wisconsin, ranked 24th.

Table 1: Index of State Economic Momentum, September 1991

Rank	State	Index	Rank	State	Index	Rank	State	Index
1	Nevada	2.89	18	Mississippi	0.73		**United States**	**0.00**
2	Utah	2.54	19	Kansas	0.71	35	Delaware	-0.03
3	Nebraska	2.50	20	Minnesota	0.66	36	Virginia	-0.23
4	Hawaii	2.09	21	Wyoming	0.63	37	Georgia	-0.25
5	New Mexico	1.78	22	Florida	0.48	38	North Carolina	-0.26
6	Washington	1.66	23	Oklahoma	0.46	39	Missouri	-0.32
7	Arkansas	1.63	24	Wisconsin	0.44	40	Pennsylvania	-0.43
8	South Dakota	1.61	25	California	0.43	41	Maryland	-0.43
9	Oregon	1.54	26	West Virginia	0.35	42	Michigan	-1.12
10	Montana	1.53	27	Iowa	0.34	43	New York	-1.57
11	Idaho	1.52	28	South Carolina	0.30	44	New Jersey	-1.63
12	Arizona	1.50	29	Kentucky	0.28	45	Connecticut	-1.75
13	North Dakota	1.49	30	Indiana	0.25	46	Vermont	-1.78
14	Texas	1.38	31	Tennessee	0.20	47	Maine	-2.11
15	Colorado	1.23	32	Alabama	0.14	48	Rhode Island	-2.22
16	Alaska	1.01	33	Illinois	0.07	49	Massachusetts	-2.71
17	Louisiana	0.74	34	Ohio	0.03	50	New Hampshire	-2.76

What are the leading states doing right? For most of them, the answer is not so much that they have done something better than other states but that they avoided some problems plaguing the low-ranking states.

First, the low ranking states generally had overheated economies in the sense that construction and real estate prices had reached unsustainable levels. Because the economies of many Western and Southwestern states were depressed in the mid-1980s and haven't fully recovered, there was no remaining economic bubble to be burst in the 1990s. Arizona, Colorado, Louisiana, and Texas are examples. Second, the economies of the winning states are closely tied to resources -- oil and gas, timber, mining, and agriculture. These industries aren't all doing well, but overall aren't doing badly. Third, the economies of the losing states are closely tied to activities like manufacturing, finance, and defense procurement, which haven't been areas of strong growth.

Success Stories

There are significant success stories in the top-ranked states, although it is difficult to say how much of the success is attributable to state government policies and how much to other factors. Nevada leads the nation, though its margin above other states has declined from the September index, proving that no state economy can massively outperform the national average for long. Washington and Oregon, fueled by new industries like software and by in-migration, have resisted the recession, though Washington is now lowering its revenue expectations as recession reaches its economy. Hawaii continues to gain from foreign investment and tourism. Idaho and Utah have been steadily moving up in the Index.

The mystery is state economic performance that cannot be explained by regional trends, industry mix, or other variables. Three of the winners -- Arkansas, Nebraska, and New Mexico -- stand out. In the losers' column, there is no similar phenomenon. Each state ranks close to states that share its geography and economic characteristics.

Employment Change

From September 1990 to September of this year, the nation lost 747,200 jobs. The pace of job change among the states was uneven, as shown in Table 2. Twenty-eight states showed some gain in employment, though it was less than 10,000 jobs in all but nine states. Twenty-two states lost jobs, with the loss over 10,000 jobs in eighteen of them.

Table 2: Change In Employment (000), September 1990 And 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Texas	74.4	18	North Dakota	6.3	35	Tennessee	-15.3
2	Nebraska	39.2	19	Ohio	5.9	36	Missouri	-18.5
3	Arkansas	26.2	20	Montana	5.8	37	North Carolina	-20.6
4	Illinois	22.7	21	Washington	5.0	38	Maine	-20.7
5	Arizona	22.4	22	Oklahoma	4.8	39	New Hampshire	-24.4
6	Utah	22.3	23	Wisconsin	4.7	40	Maryland	-33.6
7	Colorado	22.2	24	Nevada	4.1	41	Virginia	-40.2
8	Louisiana	19.3	25	Iowa	3.8	42	Connecticut	-47.1
9	Oregon	17.5	26	West Virginia	3.8	43	Pennsylvania	-47.9
10	Minnesota	9.0	27	Wyoming	2.2	44	Georgia	-57.0
11	Kansas	8.9	28	Alaska	1.4	45	Florida	-67.1
12	South Dakota	8.9	29	South Carolina	-1.1	46	Michigan	-72.5
13	Idaho	7.8	30	Indiana	-2.9	47	California	-85.3
14	Kentucky	7.6	31	Delaware	-4.2	48	New Jersey	-103.9
15	Hawaii	7.2	32	Vermont	-7.1	49	Massachusetts	-152.0
16	New Mexico	7.0	33	Alabama	-12.7	50	New York	-276.2
17	Mississippi	6.9	34	Rhode Island	-14.2			

The economy lost about 0.7% of its jobs in one year, a time span when the economy under normal conditions would show an employment increase of at least 1%. The percentage change in employment over the latest year for which data are available for all 50 states is shown in Table 3.

Table 3: Percentage Change In Employment, September 1990 And 1991

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Nebraska	5.31%	18.	Nevada	0.64%	34	Alabama	-0.77%
2	South Dakota	3.06	19.	West Virginia	0.60	35	Missouri	-0.78
3	Utah	3.03	20.	Alaska	0.56	36	Pennsylvania	-0.92
4	Arkansas	2.78	21.	Kentucky	0.51	37	Delaware	-1.21
5	North Dakota	2.35	22.	Illinois	0.43	38	Florida	-1.25
6	Idaho	1.95	23.	Minnesota	0.42	39	Virginia	-1.38
7	Montana	1.91	24.	Oklahoma	0.40	40	Maryland	-1.54
8	Arizona	1.50	25.	Iowa	0.31	41	Michigan	-1.83
9	Colorado	1.44	26.	Washington	0.23	42	Georgia	-1.89
10	Hawaii	1.38	27.	Wisconsin	0.20	43	Vermont	-2.74
11	Oregon	1.38	28.	Ohio	0.12	44	New Jersey	-2.84
12	New Mexico	1.21	29.	South Carolina	-0.07	45	Connecticut	-2.88
13	Louisiana	1.20	30.	Indiana	-0.11	46	Rhode Island	-3.15
14	Wyoming	1.06	31.	North Carolina	-0.65	47	New York	-3.36
15	Texas	1.05	32.	California	-0.66	48	Maine	-3.80
16	Kansas	0.82		**United States**	**-0.68**	49	New Hampshire	-4.75
17	Mississippi	0.73	33.	Tennessee	-0.69	50	Massachusetts	-5.14

Table 3 shows striking differences among the states. Fifteen states bucked the national trend with employment growth of 1% or more. Every one of them is West of the Mississippi River. Nebraska's economic performance was simply outstanding for a time when the rest of the nation was experiencing problems. All sectors of the Nebraska economy, from manufacturing to trade to services, gained in employment. Some formerly fallen stars -- states affected by the oil and gas depression of the mid-1980s -- are showing employment growth. Kansas, Mississippi, Louisiana, and Texas are all shown in the first column of Table 3. West Virginia, after a decade of depression, has no where to go but up and is now gaining jobs while the nationwide trend is downward.

The table suggests some new falling stars as well. Nevada's unsustainable growth has moved closer to the national average in job gains, with population and personal income growth likely to follow. California and Florida, which outperformed the nation through the 1980s, aren't maintaining this strength. While the most distressing employment losses are in the Northeast, which holds the bottom eight slots, some Southeastern states are now in the bottom third.

Personal Income Growing Slowly

While changes in job-holding are important indicators of state performance, there are many other factors affecting the income of state residents. They include compensation changes for those remaining in the same job, Social Security payments, earnings on investments, income of sole proprietors and partners, and government payments for employee retirement, agricultural price supports, and other programs. All of these are captured in the personal income measure shown in Table 4.

Table 4: Percentage Change In Personal Income, Second Quarter, 1990 And 1991

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Hawaii	7.5%	18	Oregon	5.2%	34	Delaware	3.7%
2	Utah	7.4	19	Idaho	5.1	35	Ohio	3.6
3	New Mexico	7.2	20	West Virginia	5.0	36	Illinois	3.4
4	North Dakota	7.0	21	Kansas	4.9	36	Virginia	3.4
5	Montana	6.6	21	Oklahoma	4.9	38	Pennsylvania	3.3
6	Nevada	6.1	23	Alabama	4.7	39	Missouri	3.2
7	Washington	6.0	24	Tennessee	4.6	40	Maryland	2.9
8	Nebraska	5.8	25	Minnesota	4.5	41	North Carolina	2.7
8	Texas	5.8	26	Indiana	4.3	42	New York	2.3
10	Alaska	5.7	26	Iowa	4.3	43	Michigan	1.8
10	Arkansas	5.7	28	Wisconsin	4.2	44	New Jersey	1.7
10	South Dakota	5.7	29	Florida	4.1	45	Connecticut	1.3
13	Arizona	5.6	30	California	3.9	46	Massachusetts	0.8
13	Louisiana	5.6	30	Georgia	3.9	47	Maine	0.6
15	Colorado	5.5	30	Kentucky	3.9	48	Vermont	0.3
15	Wyoming	5.5	30	South Carolina	3.9	49	Rhode Island	0.1
17	Mississippi	5.3		**United States**	**3.7**	50	New Hampshire	-0.1

The bad news in Table 4 is not so much how individual states are doing relative to each other as how bad the national total is. For the economy simply to stand in place, maintaining the purchasing power of consumers, an increase larger than 3.7% would be necessary -- 3% or so to reflect inflation and 1% to reflect population growth.

About 20 states with about half the nation's population lost ground economically during the year covered by the table. Adding 2% for normal productivity growth produces a normal growth rate target of 6%. Only seven states made this target. Those seven are less populous states, including North Dakota which bounces around in income comparisons because of the timing of federal crop support payments.

Population Change

In extreme cases, population growth and economic development are related. West Virginia, which lost population in the 1980s, clearly didn't do as well as California and Florida with their rapid gains. But population gain isn't an unmitigated blessing. If there are more people but no more jobs, per capita income will drop and unemployment will rise.

Economists can't quite agree on the exact relationship between population and development. There are three basic ties, but forecasting the correlations with other factors like personal income isn't easy. First, population movements signal economic success and failure as people move toward job opportunities and away from areas where work they want can't be found. This explains why states like West Virginia and the Dakotas have been losing population and states like Washington have been gaining population. Second, some people move oblivious to job opportunities because they are in search of climate, low living costs, or other factors. Moves of retirees to states like Arizona, Florida, and Nevada are examples. These people bring their purchasing power with them, so their movement aids a state's economy. Third, rapid natural population growth will create a pool of workers seeking employment, generally at relatively low wages. That pool can itself attract economic development, which is much of the story behind the rapid growth of the economies of Idaho and Utah.

Table 5 shows the population changes used in the Index of Economic Momentum.

Table 5: Percentage Change In Population, 1989-1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Nevada	5.72%	18	Minnesota	0.85%	34	Rhode Island	0.20%
2	Washington	2.55		**United States**	**0.77**	35	Nebraska	0.19
3	Florida	2.37	19	New Mexico	0.73	36	Illinois	0.18
4	California	1.86	20	Wisconsin	0.72	37	Ohio	0.17
5	Oregon	1.83	21	Maine	0.66	38	New York	0.15
6	Idaho	1.31	22	Colorado	0.55	39	Pennsylvania	0.13
7	Delaware	1.22	23	Alaska	0.55	40	Connecticut	0.12
8	Hawaii	1.19	24	Tennessee	0.47	41	New Jersey	0.05
9	Arizona	1.19	25	Michigan	0.45	42	Massachusetts	0.00
10	Maryland	1.14	26	Missouri	0.41	43	Mississippi	-0.04
11	Virginia	1.09	27	Indiana	0.36	44	Montana	-0.13
12	Texas	1.07	28	New Hampshire	0.36	45	Oklahoma	-0.13
13	Georgia	1.05	29	Alabama	0.27	46	South Dakota	-0.14
14	Utah	1.00	30	Kentucky	0.22	47	West Virginia	-0.77
15	North Carolina	0.97	31	Iowa	0.22	48	Louisiana	-0.78
16	Vermont	0.90	32	Arkansas	0.21	49	Wyoming	-0.87
17	South Carolina	0.87	33	Kansas	0.20	50	North Dakota	-1.08

These data (which cover nine months as explained in the Technical Notes) reflect about a 1% annual increase in population nationally. They show massive differences among the states. Eight states lost population while many of the Northeastern and Midwestern states showed increases of less than half the national average. This slow growth correlates with several factors affecting state policy including: (1) a rising average age, (2) shrinking school enrollment, and (3) a decline in the 18-25 age group that is the major source of both college attenders and criminals.

Population Change And State Spending Pressure

The population growth statistics are indicators of demographic pressures on state spending. Table 6 shows that eight states account for about 75% of the total national population increase.

Table 6: Population Growth In Fast Growing States, 1989-1990

State	Population Increase (000)	Cumulative Percent Of U.S. Increase
California	542	28.7%
Florida	300	44.6
Texas	180	54.1
Washington	121	60.5
Virginia	67	64.0
Georgia	67	67.6
Nevada	65	71.0
North Carolina	64	74.4
United States	**1,890**	**100.0%**

The eight states shown as accounting for three fourths of the population increase now have only about a third of total U.S. population. There are significant policy differences associated with these demographic characteristics. One is concern with U.S. immigration policy and who bears the consequences of that policy. When California legislators and the governor met recently on the state's latest budget gap, they didn't agree on how to close it. They did agree to seek federal policy changes to ameliorate the impact of legal and illegal immigration on the state's budget. Much of California's rapid population growth is from immigration with easily identifiable impacts on state costs for elementary and secondary education, welfare, and health and social services.

The high growth states have serious infrastructure capacity problems. Traffic congestion in California and Houston are nationally-known. There are similar problems along Florida's coasts, in the Seattle area, and in Northern Virginia. There are school construction backlogs conservatively priced in the billions in California and significant problems in meeting demand at all levels of education in many of the rapid growth states. In the major metropolitan areas of the Northeast and Midwest, there are concerns about infrastructure, but key indicators of demand -- students in school, transit trips, vehicle miles traveled -- are often below what they were in peak years. As a result, maintenance is more a concern than expansion of capacity, though there is always someone interested in adding capacity.

Consumers Take A Holiday

As has been widely reported, the American consumer has been reluctant to spend. Nationally, retail sales growth has been an anemic 1% from the first nine months of 1990 to the same nine months of 1991. The state-by-state information, which is available only for 20 of the largest states, appears in Table 7.

Table 7: Retail Sales Growth, Nine Months, 1990 And 1991

State	Percent	State	Percent	State	Percent
Indiana	6.8%	Illinois	1.9%	New Jersey	-0.6%
Minnesota	5.8	Missouri	1.5	New York	-1.2
Florida	5.4	North Carolina	1.4	California	-1.5
Texas	5.3	Massachusetts	1.4	Wisconsin	-2.6
Ohio	4.6	**United States**	**1.0**	Pennsylvania	-2.9
Tennessee	2.4	Michigan	0.7	Virgiinia	-4.9
Louisiana	2.0	Maryland	-0.4		

These data, which are less reliable than information on employment and personal income, show extremely wide variations among the states. They confirm the other indicators in showing poor economic performance in the Northeast and California, but show somewhat more strength in the Midwest.

Housing Markets Weak Nationally

Housing and commercial construction are highly volatile components of state economies, particularly in states that have been experiencing rapid growth. Economic gains tend to create the expectation of more gains for those moving quickly. So speculative building is common in high growth areas. But when growth slows, builders and investors discover that the market may be overbuilt. In the adjustment phase, construction activity drops below what a "normal" pace might be as builders wait for demand to sop up what they call the overhang of empty office space and residential units. Table 8 reflects this phenomenon, which appears in the change in the issuance of permits for new residential units.

Table 8: Building Permits Growth, Nine Months, 1990 And 1991

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	North Dakota	38%	18	West Virginia	-6%	35	Delaware	-18%
2	Alaska	24	19	Wisconsin	-6	36	Illinois	-18
3	Utah	24	20	Kansas	-8		**United States**	**-19**
4	Colorado	22	21	North Carolina	-8	37	Massachusetts	-20
5	Louisiana	20	22	Connecticut	-11	38	Michigan	-20
6	Montana	20	23	South Carolina	-11	39	Virginia	-21
7	Hawaii	15	24	Alabama	-12	40	Rhode Island	-23
8	Oklahoma	11	25	Georgia	-12	41	Maine	-26
9	Idaho	10	26	New Mexico	-12	42	South Dakota	-26
10	Wyoming	7	27	Tennessee	-12	43	Florida	-28
11	Iowa	3	28	Minnesota	-13	44	Nevada	-28
12	Texas	2	29	Ohio	-14	45	New Hampshire	-28
13	Arkansas	-1	30	Mississippi	-15	46	Maryland	-29
14	Pennsylvania	-2	31	Nebraska	-16	47	Washington	-31
15	Arizona	-3	32	Kentucky	-17	48	New Jersey	-33
16	Indiana	-4	33	New York	-17	49	Oregon	-38
17	Missouri	-5	34	Vermont	-17	50	California	-40

The table deals with change in building activity, not total building activity. Many of the states that beat the national average -- such as Indiana, Missouri, and West Virginia -- don't have high levels of building activity by such measures as new units being built per 10,000 households or construction workers as a percentage of population. They do have stable activity, which is why they do better than the national average of a 19% decline. Most of the states in the center column of the table show this pattern of stability. The states with increases, as shown in the first column, are like those which lead the Index of State Economic Momentum, smaller states in the West.

The ten states with a drop of 25% or more have the most significance for state economies because the decline has been so dramatic in a market where housing construction has been a major force. California is at the bottom with a 40% decline. This means that roughly two out of every five people building new residential housing last year are out of a job this year. Similar declines will be affecting settlement attorneys, title searchers, drapery fitters, and others whose business is closely related to new housing construction. Florida and Nevada, two states that have escaped some of recession's impacts, are also near the bottom of the list.

The National Association of Home Builders sees rocky times ahead in home building. It figures the total construction job loss over the past two years has been 650,000. The unemployment rate among construction workers has reached 16%. The Association expects that homebuilding, as measured by Table 8, will get worse before it gets better.

THE ECONOMY AND STATE FINANCES

The New Year, Deja Vu All Over Again?

The condition of the nation's economy will play a critical role in state policy over the next several months. Practically all states face about the same problems.

Economic performance in the second half of 1991 has been worse than just about everyone expected. As a result, state spending is higher than expected. As a result, revenues are lower than expected. As a result, state finances are in worse shape than expected.

IF signs of recovery appear quickly, state elected officials will have a sporting chance of fulfilling their expectations for state policy and their commitments to the electorate. These often include not raising taxes, keeping pressures off local property taxes, and funding improvements in government activities like education. The situation may be tight, but the beginnings of recovery lend credence to policies, such as use of one-time revenues and delaying bill payments, that make little sense if economic stagnation will continue for a long time.

IF there isn't light to be seen at the end of the tunnel, there will be strong pressures for the election-year decisions elected officials least like -- tax increases and/or sharp spending cuts.

There Is No Sign On The Bottom

Economic forecasting is never particularly reliable. As California's legislative fiscal officer told legislators at a recent hearing, it is particularly difficult to forecast the timing of recovery from recession.

Errors in finding the economic bottom are hazardous for makers of state policy, no matter what type of error is made.

Erroneously forecasting turnarounds that don't occur leaves states long on spending and short on revenues. This is the circumstance in which officials of most states find themselves today.

Erroneously predicting that recovery won't occur leads to tax increases that are too large for what turns out to be the situation and to spending cuts that, in retrospect, are excessive. This happened in some states, particularly in the Midwest, in the 1981-1982 recession. State tax increases were bunched in December of 1982 and early 1983. They generated more revenue than needed to fund long-term spending levels and more taxpayer resistance than elected officials found acceptable. Some were rolled back.

The Budget Outlook

In most states, the outlook is for no costly new initiatives in the new FY 1993 budgets. For schools, this means inflation adjustments at best, with new education quality moves confined to those involving little cost such as school governance reforms and student testing. Past legislation calling for more than this may not be funded. For higher education, this means another year, like FY 1992 (Issue 23), with state support below or at inflation.

For welfare, it means little or no increase in payment levels. For welfare and Medicaid, it means no increase in eligibility except as required by federal law. For corrections, it means current service funding in some states and attempts to reduce growth in inmate populations by alternative sentencing and early release in others. For local aid, it means no new programs and some pressure to cut existing ones. For all other programs, it means current service funding, often adjusted by small across-the-board percentage cuts.

For taxpayers, prospects for major tax relief are dim. Less costly relief measures will be considered. Examples are industrial development incentives, business research and development and investment credits, and attempts to lower taxes of low-income wage earners. Some could be adopted, but not many. Election-oriented legislators will offer many more costly relief measures -- a penny off the sales tax, new sales tax exemptions, new income tax credits -- but these are likely to end their legislative careers in committee.

There will be exceptions. Some states, such as Kansas and Tennessee, may increase taxes enough to fund new initiatives just as Pennsylvania did this year. Litigation on school finance could force action in some states. But, in general, the situation will be tight.

States Bucking The Trend?

Will there be exceptions because some state economies are clearly outperforming the nation? Probably not many, as suggested by the new Index of State Economic Momentum (Table 1).

Only four states are 2% or more above the national growth rate in the Index. Each has its own problems. Nevada (ranked #1) is paying the price of the rapid population growth that leads to its top ranking. Its lucrative gambling base is being spread over a larger and larger population, which increasingly includes families with children in school and looking for college openings. State taxes were raised this year. A recent review of state finances in the 1990s predicted more increases would prove necessary. Utah (#2) has the nation's highest birth rate and faces resulting needs for school construction and operations spending. Part of its economic success is based on a reasonably well educated and motivated labor force, but it will likely use its prosperity to try to keep education spending, as indicated by class sizes, from being too far out of line with other states.

Nebraska (#3) has a unique set of problems related to property taxes, particularly personal property, that may result in a substantial overhaul of its tax system. If relative prosperity generates extra revenues, facilitating that change will probably get first call on its resources. Hawaii (#4) is experiencing two major problems associated with its prosperity: (1) congestion in the Honolulu area and (2) housing prices that are out of sight for many of its citizens. Expensive plans for dealing with one or the other will probably take priority over decreasing tax burdens.

State Policies To Stimulate The Economy

> *I think he's sensing that the taxpayer, the citizen, wants government to show some leadership in the area of economic recovery. He's talked about it more and more in the last few weeks.*

This comment about a governor's thinking made by his communications director is typical of the discussion in state capitols about what to do about the recession. But Minnesota's Governor Carlson, like other governors, finds his options are limited. Traditional economic stimulus measures involve putting more purchasing power into the hands of taxpayer/consumers by lowering taxes or raising spending. Balanced budget requirements force states to take away in higher taxes (or lower spending) what they put in by higher spending (or lower taxes).

Revenue neutral plans, such as raising income taxes on the rich to pay for tax relief for middle income taxpayers, may be desirable on other grounds but have little stimulative effect. Such plans, suggested by some lawmakers in Congress and the Minnesota legislature, will have slight stimulus because the savings rate is higher for higher income people, so the tax change will draw some money from savings to spending.

The options with the most impact spend money raised from borrowing and/or cash reserves. In many states, there has been discussion of accelerating highway and other construction financed by bond issues. There has been some acceleration, but until Congress acted on highway legislation it was difficult to accelerate highway projects.

States As The Economic Villain

State governments themselves aren't adding to consumer confidence. The normal course of state budget balancing activities leads to many bad-news headlines.

State faces deficit, tax increases discussed.

Layoffs, payless paydays, threatened in state government.

School district faces cutbacks, layoffs, as state aid reduced.

Nursing home threatens shutdown as state payments delayed.

No raises next year, governor warns state employees -- mayor cautions city workers.

This kind of news tends to undermine confidence of those who are not directly affected as well as those who are. For those who are affected and in turn those affected by them, the results are comparable to similar moves in the private sector. Layoffs and decisions not to fill vacancies create the same income losses whether the employer is in the private sector, the state, or a local government affected by state aid changes. Even welfare matters. As Washington's chief economist recently pointed out, "A dollar spent in the grocery store by a welfare mother is no different than a dollar spent by a Boeing worker."

FEDERAL IMPACTS ON STATE FINANCES

Introduction

By the standards of the past three decades, state officials continue to experience a period of extraordinary stability in federal policies affecting the management of states.

Overall Policy And Economic Management

The work of state officials would be easier if the federal government solved the nation's problems -- providing affordable and accessible health care, stemming the flow of illegal drugs, reducing crime, reducing teen pregnancy and dependency, and dealing with AIDS. If the federal government isn't to solve these and other problems directly, many believe it should provide more aid to state and local governments being expected to solve them. State officials of all political persuasions often suggest more federal action. Governor Cuomo's case is one of the broadest and best known. There are many narrower ones, such as the bipartisan California position that the federal government should bear a greater share of the costs of its immigration policies.

State finances are largely at the mercy of the success of national economic management. Against a standard of sustained 3% growth in the national economy, federal economic management is the cause of a major part of current state fiscal difficulties and more successful economic management would solve most of the problems.

In these broad aspects, there are few state problems that can't be blamed on the federal government. From time to time, state officials do lay this blame. But in contrast to the 1960s, state officials aren't waiting for federal action. Much of their immediate interest is in less broad aspects of federal policy like taxes, grants, Medicaid rules, and mandates.

Possible Federal Tax Policy Changes

Introduction: In the early 1980s, there was great uncertainty about federal tax policy. Changes were frequent and future policy highly uncertain because of pending tax reform legislation. Following enactment of the federal tax reform legislation of 1986, there has been a broad consensus that major federal tax issues shouldn't be reconsidered anytime soon. The argument is that stability in tax policy has so many benefits that it should be preferred for a time to any changes no matter how meritorious. This view is so widely held that legislation to extend certain expiring provisions (e.g., low income housing credit and mortgage revenue bonds) was enacted quietly this year in the closing minutes of the session to discourage opening up other policy issues.

In the discussion of how to deal with recession, many Members of Congress have offered tax cutting ideas. The President is expected to do so in January. Prospects are uncertain. First, there is still reluctance to open complex provisions of the tax code, such as treatment of income from investments. Second, there is reluctance to experience revenue loss given a deficit involving $1,000 in new federal debt per American per year. Third, the President and Democrats in Congress may be unable to agree on what changes to make. In general, the proposed changes wouldn't cause major changes in state tax laws or revenues, but would have some impacts as described below.

Business Tax Changes: The discussion of business tax incentives has centered on those, like an investment credit, that are taken after the basic tax liability is calculated. States already have a pattern of corporate tax credits bearing little resemblance to federal credits. They wouldn't necessarily make the same changes as those made at the federal level. But proposals to allow faster write-off (depreciation) of business machinery and equipment would reduce taxable income, at least in the short term, and thus reduce corporate income tax revenue of state and federal governments. When a comparable change was made a decade ago, some states conformed immediately, but many delayed conformity to cushion the revenue loss.

Tax Credits For Individuals: One plan, proposed by House Ways and Means Chairman Rostenkowski, would provide a credit of 20% of federal payroll taxes for Social Security and Medicare with a limit of $200 per individual. Senate Finance Chairman Bentsen would give a $300 per child credit. These would have no direct effect on state tax policy or revenues.

Rate Changes: Excepting a few states like Vermont that base state tax liability on federal liability, state taxes are independent of federal tax rates. So plans, like Rostenkowski's, that would raise top bracket rates would have no impact on states.

Retirement Accounts: Several plans are designed to encourage individual savings in IRAs and other retirement accounts. One mechanism is to reduce the limits on contributions (e.g., amounts, who can contribute) which would reduce taxable income and thus tax revenue. Another is to expand the circumstances under which money can be taken out without penalty for early withdrawal. Both approaches would affect the state as well as federal tax base.

Capital Gains: The tax reform legislation ended a decades-old pattern of lower taxes on capital gains than other income. Some people argue the change reduced incentives to invest and American productivity and competitiveness. The likely change is to reduce the amount of gain that is taxable, which would reduce the income tax base of conforming states. A few states (e.g., Wisconsin) retained special capital gains treatment and wouldn't be affected.

Passive Losses: One of the major changes in the 1986 reform legislation was to prevent the offset of income by real estate and other tax shelters (passive losses). This decision would be altered by some of the proposals, cutting taxable income and thus state as well as federal revenue.

Interest Income: One of the proposals would allow exclusion of interest income up to $225 for individuals, leading to a loss for both federal and state treasuries.

Possible Major Spending Changes

The continuing deterioration of the political and economic situation in the Soviet Union is leading many Members of Congress to eye the prospects for a defense dividend that might result from a faster scaledown of defense spending than is contemplated by the multi-year agreement on the federal budget. It isn't obvious that such a reduction in defense spending will occur or that, if it does, the resources would be redirected to programs directly affecting state policy. Other alternatives include deficit reduction, federal tax reduction, and direct federal outlays for such functions as health research, foreign aid (including aid to the Soviet Union), pollution control and clean up at federal facilities.

State and local governments have fared well recently, if this can be measured by growth in federal grants. In the third quarter of 1991, federal grants to state and local governments were being made at an annual rate of $152 billion a year. This was up $22.2 billion from the same quarter a year earlier, an increase of 17.1%. At the same time, overall federal spending only increased 5.2%. Medicaid was the driving force in the rapid grant increases. The results in the new federal budget are indicated by Table 9 which lists programs of interest to states with FY 1992 funding in excess of $1 billion.

A compilation of grant funding by Federal Funds Information for States shows grants rising to $185.4 billion in FY 1992, a rise of $27.2 billion from $158.2 billion in the current year. This increase of 17.2% is well above what state and local governments will raise for themselves (6-8%) and likely inflation (3-5%).

Table 9: Major Federal Programs Affecting State Governments
FY 1992 Appropriations ($ billion) And Change From FY 1991

Program	Amount	Percent Change
Medicaid Benefits And Administration	$68.1	29.5%
Food Stamp Benefits	20.7	14.9
Highways (Obligation Ceiling)	16.8	15.9
Welfare (AFDC) Payments	12.2	7.4
Compensatory Education (Chapter 1)	6.8	10.0
Community Development Block Grants	3.4	6.3
Social Service Block Grants	2.8	0.0
Women, Infants, and Children (WIC) Program	2.6	10.6
EPA Water Pollution Construction Grants	2.4	14.3
Head Start	2.2	12.8
Special Education Basic Grant	2.0	6.6
Low Income Home Heating Assistance	1.5	-6.8
Alcohol, Drug Abuse, and Mental Health Grant	1.4	7.2
Vocational and Adult Education	1.4	14.8

If state and local officials were given the option to spend any defense dividends, they would be able to develop a long list of desired programs. Past policy pronouncements and current fiscal circumstances suggest that state officials would emphasize means-tested programs. Federal assumption of health care responsibility would probably top the list, starting with long-term care (nursing homes, hospices, home health care) for the aged. Federal acceptance of a cost item of this magnitude would, at least for a time, remedy the tight fiscal condition in which most states now find themselves. However, relief from this source isn't being assumed in state budgets.

Mandate Relief

Quantifying the impact of federal mandates on state and local budgets remains a formidable task, though NCSL is now quantifying the cost impacts of proposed new federal mandates. The most visible mandates are the most recent ones because they are discussed in connection with state budgets. Major examples include: (1) the extension of AFDC eligibility to two-parent households, (2) the extension of Medicaid to certain pregnant women and young children, (3) Medicaid coverage of costs of low-income persons over 65 for costs not covered by Medicare, (4) Medicaid reimbursement rates for hospitals and other health care providers, and (5) rights of institutionalized persons enforced through litigation involving prisoners, mental health patients, and others.

In terms of total cost impact, some less discussed mandates adopted years ago but now having their greatest effects may be more significant. Water pollution control standards, particularly separation on storm and sanitary sewers, are one example. Laws affecting solid waste disposal and landfills are also big money items.

These costs are local rather than state, but many states have agreed to share them. Fiscal circumstances in some states, such as Massachusetts, have put limits on state ability to provide the cost sharing previously promised for local projects.

Medicaid Finance

Not everyone was equally thrilled by the compromise enacted by Congress on Medicaid bootstrap financing. NGA's executive director called it a victory for the states. NCSL's Federal Update (12/6) noted the settlement was "prompted by the willingness of the National Governors' Association to compromise state taxing authority and disproportionate share hospital payment practices."

The assessment in part depends upon the starting point for analysis. Assessed against state practices as they existed in the summer of 1991, the settlement provides major new sources of fiscal flexibility and budget relief for all but a few states. Assessed against present state practices, it provides new sources of fiscal relief for most states and protects the fiscal flexibility already seized by most of the others. But assessed against the potentials if every state did what the most aggressive states have done, there is a substantial loss in potential flexibility.

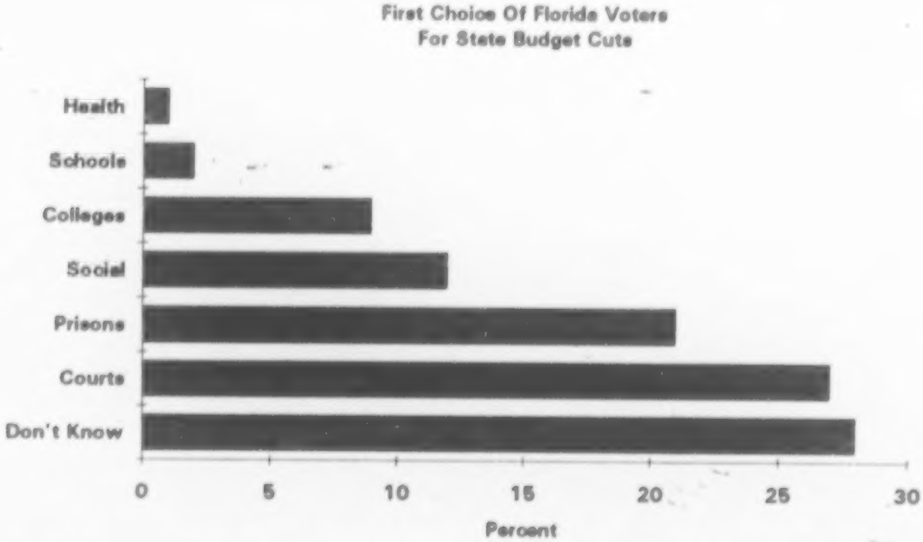
The immediate news is all good. Many states used bootstrap financing to avoid or minimize sharp cuts in their FY 1992 budgets, accepting risks of federal disallowance so great that other states were reluctant to try the tactic. The aggressive strategy is working for FY 1992. The FY 1993 budgets can be expected to use this flexibility again, thereby mitigating budget pressures from Medicaid.

PUBLIC OPINION

Public opinion polls continue to show that the public likes spending but doesn't like taxes. But when it comes to closing budget gaps, the combination of lower spending and higher taxes seems to have much appeal.

In Florida, there has been considerable fanfare about budget cuts. The FY 1992 budget was viewed as tight before it was enacted. Press reports were filled with dire predictions of cutbacks. In the fall, the governor announced that the FY 1992 budget was out of balance by over $600 million. He endorsed 5.4% cuts in many programs. Subsequently, Florida courts decided the action exceeded his power, so a special legislative session is being held to deal with cutbacks.

In October, Florida voters were asked how state government should deal with its money shortage. Only 11% chose raising taxes, 34% said cut spending, 46% picked a combination of the two, and 9% didn't have an opinion. Respondents were asked to think about their local school system if faced with a 10% cut. Only 14% said "the only way it can do so is by laying off teachers -- and hurting the overall quality of education." Nine percent weren't sure and 77% picked the statement: "My local school system could easily cut its budget by 10% -- without hurting the overall quality of education -- by laying off administrators instead of teachers." On state cuts, there was a clear preference as shown in the graph. The question was, "If the state must cut, which area would you cut most?"



About half the Florida voters said the possibility that they would support higher taxes was increased by hearing of the budget cuts. But only 20% favor an income tax. This percentage rises to 44% if the income tax would only be on income over $75,000 a year. Doing something specific with new taxes was a hit with Maryland voters in a survey sponsored by the Maryland State Teachers Association. A tax increase to close the budget shortfall got about one-third support, but 76% support appeared for a tax increase associated with education.

The Iowa Poll has established that 56% of the state's voters disapprove of the laying off of state workers, but only 31% support a tax increase to avoid layoffs. Iowa has been cutting state support for universities. To address the resulting budget problems, only 13% favor substantial tuition increases and only 22% favor elimination of academic programs. A salary freeze splits the electorate. More state tax support is favored by a two-to-one margin.

COMPARING AFFLUENCE AMONG THE STATES

Despite their economic problems, Northeastern states continue to lead the nation in affluence in 1990. But they may soon see their lead erode.

Per Capita Income Differences

As shown in Table 10, only three states -- Connecticut, New Jersey, and Massachusetts -- were 20% or more above the national average in per capita income. Six states were more than 20% below average. At one time, states of the Old South monopolized the bottom positions. Now three of the bottom five positions are held by states outside the South. New Mexico and, especially, Utah are there because of rapid population growth, the denominator in per capita income. West Virginia's problem is low income, not population growth.

Table 10: Per Capita Personal Income 1990

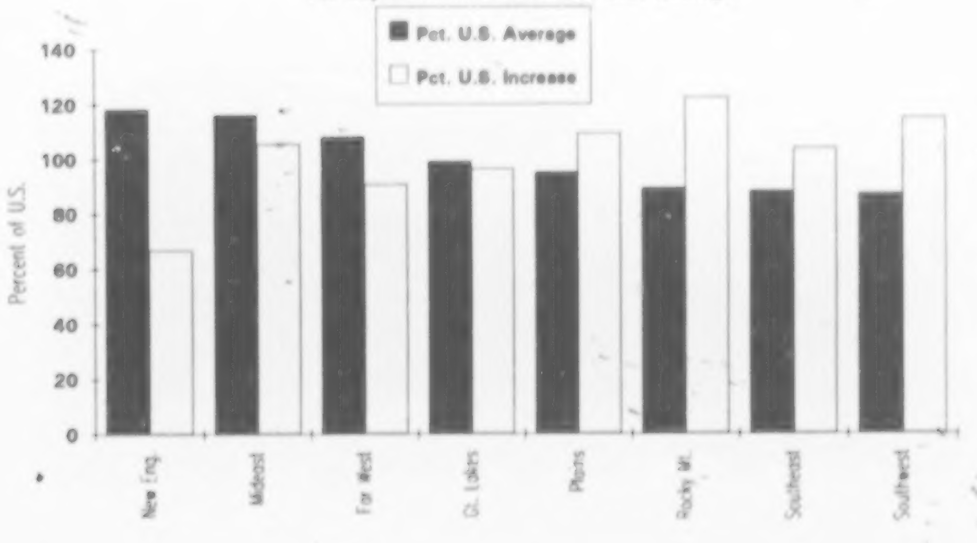
Rank	State	Amount	Pct. of US	Rank	State	Amount	Pct. of US
1	Connecticut	$25,484	136%	26	Missouri	$17,472	93%
2	New Jersey	24,936	133	27	Iowa	17,218	92
3	Massachusetts	22,569	121	28	Oregon	17,196	92
4	New York	22,086	118	29	Maine	17,175	92
5	Maryland	21,789	117	30	Georgia	17,049	91
6	Alaska	21,688	116	31	Indiana	16,890	90
7	New Hampshire	20,827	111	32	Texas	16,716	89
8	California	20,677	111	33	Wyoming	16,314	87
9	Illinois	20,419	109	34	North Carolina	16,293	87
10	Hawaii	20,356	109	35	Arizona	16,012	86
11	Delaware	20,022	107	36	Tennessee	15,866	85
12	Virginia	19,671	105	37	South Dakota	15,797	85
13	Nevada	19,035	102	38	Oklahoma	15,457	83
14	Colorado	18,890	101	39	Montana	15,270	82
15	Rhode Island	18,802	101	40	Idaho	15,249	82
16	Washington	18,775	100	41	North Dakota	15,215	81
17	Minnesota	18,731	100	42	South Carolina	15,151	81
	United States	**18,691**	**100**	43	Alabama	15,021	80
18	Pennsylvania	18,686	100	44	Kentucky	15,001	80
19	Florida	18,530	99	45	Louisiana	14,542	78
20	Michigan	18,360	98	46	New Mexico	14,265	76
21	Kansas	18,162	97	47	Arkansas	14,188	76
22	Ohio	17,564	94	48	Utah	13,993	75
23	Wisconsin	17,560	94	49	West Virginia	13,755	74
24	Nebraska	17,549	94	50	Mississippi	12,823	69
25	Vermont	17,511	94				

Only five states are from 10% to 19% ahead of the national average while 13 states are this far behind the national mark. Twenty-two states are within 10% of the national average as calculated by the Department of Commerce.

Reducing Per Capita Income Disparities

In the American economy, people are free to move to the most economic opportunity they can find and businesses and thus jobs are free to move to the places offering the best opportunities to hire workers. As a result, a state shouldn't be able to stay far above or below national averages for long, at least this is what the "convergence theory" holds. By that theory, wide differentials among states will tend to disappear over time.

Last year was an illustration of convergence at work. The chart below shows the regions of the U.S. with the solid bar representing their per capita incomes in 1990 as a percent of the national average. The other bar reflects the percentage increase in per capita income of that regional relative to the national percentage increase. For example, New England was 18% above the national average, but its growth of 3.6% was well off the national pace of 5.4%. The chart shows a definite tendency for the best growth to be found in regions with the lowest incomes. Such a pattern, if repeated year after year, would draw all the states toward the national average.


Per Capita Income Relative To U.S. Average

Migration Of The Affluent

Twenty-three years ago Allied Van Lines decided that its records on interstate moves provided a significant demographic and economic indicator. The moves in 1990 provided two firsts. For the first time, Florida dropped out of Allied's category of magnet states, which it defines as having at least 55% of all moves into the state. California had more outbound than inbound moves in 1990, also for the first time since the recordkeeping began. The information for all 50 states appears in Table 11.

Table 11: Percentage Of Allied Van Line Moves That Were Inbound, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Nevada	69.0%	18	Texas	54.7%	34	Ohio	46.6%
2	Oregon	66.7	19	Utah	54.3	35	Oklahoma	46.0
3	Maine	66.5	20	Missouri	53.2	36	Virginia	45.5
4	Hawaii	61.7	21	Arkansas	52.3	37	Illinois	45.4
5	Georgia	61.6	22	Delaware	52.3	38	Louisiana	45.3
6	Washington	61.4	23	Idaho	52.2	39	Indiana	45.2
7	Vermont	59.7	24	Kentucky	51.1	40	Michigan	45.1
8	Alaska	59.6	25	Tennessee	51.1	41	Pennsylvania	44.6
9	South Carolina	59.2	26	Minnesota	50.8	42	California	44.1
10	North Carolina	58.1	27	Wisconsin	50.6	43	Wyoming	42.4
11	Montana	57.8	28	Nebraska	50.4	44	Massachusetts	41.9
12	Colorado	57.3		**United States**	**50.0**	45	New Jersey	41.0
13	New Mexico	56.1	29	Kansas	49.8	46	New York	41.0
14	Alabama	55.9	30	West Virginia	49.8	47	New Hampshire	40.9
15	Arizona	55.9	31	Mississippi	48.8	48	South Dakota	40.9
16	Rhode Island	55.3	32	Iowa	48.5	49	Connecticut	39.8
17	Florida	54.8	33	Maryland	48.2	50	North Dakota	28.1

The data show a correlation with the Index of State Economic Momentum (Table 1), but not a perfect one. Nevada leads the Index and leads in the percentage of inbound moves. Other states showing a high percentage of inbound moves do well on the Index, such as Oregon and Hawaii. But Maine and Vermont are high in inbound moves but low on the Momentum Index.

Farm states losing population overall, like the Dakotas, have low rankings in Table 11, as would be expected. But it also shows relatively dramatic losses in other states, particularly Connecticut, New Hampshire, and Massachusetts. Large industrial states -- such as California, Illinois, Michigan, and Pennsylvania -- all are exhibiting some loss of population through Allied Van line moves, but the loss isn't dramatic.

Movement Of Retirees

Retirees have long been a major factor in Florida's growth and have something to do with Nevada's Number One ranking on the Index of State Economic Momentum. Considerable effort is being made by some states to draw retirees. In other states, there is debate over whether state policies are driving retirees away. For example, whether to eliminate an estate tax larger than those of most states is a current issue in Massachusetts.

The persons who will reach age 65 during the 1990s were born in the Depression Era when birth rates were low. So despite greater longevity, the number of persons aged 65-74 will grow by only 3% in the first half of this decade. It will fall by about the same percentage in the second half. As a result, any state expecting to get much of a gain in population in this age group will need to pick up population from other states.

A recent projection appearing in American Demographics (December) indicates that the largest gains in population of this age group during the 1990-1995 period will be in two states. Of the estimated growth of 671,527 people, California is predicted to get 216,069 and Florida to get 172,297. But when the increases are put in percentage terms, some other states show significant gains, as reflected in Table 12. A dozen states show losses in this age group.

Table 12: Estimated Percentage Growth In Population Aged 65-74, 1990-1995

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Nevada	18.0%	18	Virginia	4.3%	34	Kansas	0.6%
2	Florida	12.3	19	Utah	3.5	35	Wisconsin	0.1
3	Arizona	11.4	20	Tennessee	3.3	36	New York	0.0
4	Hawaii	11.1	21	Texas	3.3	37	Ohio	0.0
5	California	11.0		**United States**	**3.0**	38	Pennsylvania	-0.1
6	New Hampshire	9.3	22	Alabama	1.8	39	Illinois	-0.2
7	Washington	8.0	23	Rhode Island	1.8	40	Mississippi	-0.2
8	Delaware	7.9	24	Arkansas	1.7	41	South Dakota	-0.5
9	Georgia	6.0	25	Minnesota	1.5	42	Nebraska	-0.7
10	Alaska	5.9	26	Idaho	1.4	43	Kentucky	-1.1
11	New Mexico	5.9	27	New Jersey	1.3	44	Montana	-2.1
12	Vermont	5.6	28	Massachusetts	1.1	45	Iowa	-2.7
13	North Carolina	5.5	29	Indiana	0.9	46	Louisiana	-3.0
14	South Carolina	5.4	30	Connecticut	0.8	47	Oklahoma	-4.1
15	Maryland	5.3	31	Missouri	0.8	48	West Virginia	-6.3
16	Oregon	4.8	32	Colorado	0.7	49	North Dakota	-7.1
17	Maine	4.7	33	Michigan	0.7	50	Wyoming	-7.5

TECHNICAL NOTES

Index of State Economic Momentum: The Index is published quarterly in **Reports**, with the previous one appearing in Issue 18. The index is the average of three differences -- the difference between each state's change and the national change in population, personal income, and employment. Data on each of the components appear in this issue. Employment data are published monthly by the Bureau of Labor Statistics. Personal income data are published quarterly by the Bureau of Economic Analysis of the Commerce Department.

Population: Between the 1980 Census and the 1990 Census, the Census Bureau has issued annual estimates of state population. These have been used for many purposes including private and public sector analyses of markets and programs, administration of federal grants, and the Index of State Economic Momentum. The count of the 1990 Census was inconsistent with the earlier estimates, showing implausible growth and decline for some states between the last estimate and the count. So Census retrospectively redid the estimates, providing the data used in the tables and in preparation of the Index. The shift to the newer estimates affects the Index rankings of the states compared with the Index last quarter. The shifts don't appear to have been systematic. That is, they don't uniformly increase the rankings of fast or slow growing states, or states in a particular region.

Retail Trade: The Census Bureau retail trade numbers are widely used as a national economic indicator, although some economists have doubts about the accuracy of the series on a national basis. These concerns are magnified for the state-by-state data presented in Table 7.

Building Permits: The issuance of building permits doesn't mean that construction will follow, as builders may not use permits in a soft home building market. But covering nine months, as Table 8 does, should overcome criticism of use of this economic indicator.

Federal Impacts: Table 9 is taken from NCSL Federal Update (12/6). Some of the programs included, such as Food Stamp benefits, aren't counted as grants to state and local government. **Reports** took all programs listed by NCSL with FY 1992 funding over a billion except the new housing program (HOME Investment Grants) which rises from zero to $1.5 billion but replaces a variety of other housing activities being eliminated or cut.

Public Opinion: The Florida poll was sponsored by the Miami Herald which reported it on October 18.

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STATE POLICY REPORTS

VOLUME 10 ISSUE 1

IN THIS ISSUE

State fiscal situations now look poor throughout the nation, as expected recoveries in the economy and state revenues fail to appear. The result is likely to be another year of austere budgets.

- Another Tight Year p. 2

Some experts expect the fiscal problems to last a decade. California projections confirm national predictions. The predictions suggest a worse environment in the 1990s than in the 1980s for taxpayers and state-funded activities, particularly education.

- The Perpetual Fiscal Crisis? p. 6

In making fiscal adjustments, states are hurting some group: the poor? the middle class? Not everyone agrees. A new report suggests the poor, but indicates major differences among states.

- Sticking It To The Poor p. 10

While predictions of tight budgets roll in, so do data on past spending and tax burdens. There is a new list of which states have the highest and lowest taxes and spending. Some states have shown increases well above the national average. Overall state financial patterns in FY 1990 differed little from those a year earlier.

- Spending And Tax Levels p. 14

"Balance" in state tax systems isn't found in all states, but there are strong pressures for states out of line to move closer to national patterns.

- Balance In State Tax Systems p. 20

Miscellany covers college savings programs, health care, state and local fiscal interactions, urbanization, and more. Technical notes detail sources and calculations.

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- Technical Notes p. 24

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January 1992 (First Of Two January Issues)

ANOTHER TIGHT YEAR

Introduction

With no sign that the economy has hit bottom, state finances continue to deteriorate. The typical state's budget for this year (FY 1992) is in worse shape than when enacted. The reasons: (1) balances coming out of FY 1991 that were below expectations, (2) revenues, particularly in the sales tax, running below predictions, and/or (3) higher-than-expected spending for Medicaid and often other programs such as AFDC and corrections. The same factors causing problems in FY 1992 are expected to cause imbalance in FY 1993 unless taxes are increased or current spending patterns sharply curtailed. While not all states exhibit the typical pattern, most do.

Current Year Problems

There are current year shortfalls in over half the states. The worst cases are in large states like California, Florida, Illinois, Michigan, New Jersey, and New York. The exceptions are in sparsely populated states in the West. Probably, three-fourths of the nation's population lives in states with major budget problems this year.

Solving Current Year Problems

Although notions of sound state financial management and, often, state law call for correction of imbalances during the year, this isn't always happening.

In some states, the likely shortfall hasn't officially been recognized by the executive branch, so there is no legal requirement to deal with the problem. Examples are Illinois, Michigan, and New Jersey.

In some states, such as Alabama and Arkansas, corrective action is nearly automatic as spending is proportionally reduced to conform to revenues (Alabama) or reduced pursuant to a plan incorporated in the appropriations legislation (Arkansas).

In many states, the governor has sought to take corrective action, but success has been limited. In two states (Florida and Montana) where the legislature has given the governor responsibility and power to make a wide range of cuts, state courts have determined the action to be an unconstitutional delegation of legislative powers. These governors have had to turn to their legislatures for approval of proposed cuts.

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The power of the governor alone to make cuts in other states is often limited by special requirements mandating that any cuts be equal across-the-board, exempting certain programs, or making other restrictions. In all but a few cases, the executive power to make reductions doesn't extend to modifying statutes dealing with such subjects as distribution formulas for school aid and entitlements to state aid for legally designated groups.

Collective bargaining agreements also constrain executive -- and in some cases legislative -- power to make changes affecting previously negotiated agreements with employees. California and Connecticut are major examples. In these states, assumptions about pay and other compensation built into the enacted budgets aren't being realized.

As a result, many governors have turned to the legislatures to adopt their budget cutting recommendations. This mechanism was used effectively late in 1991 in Florida, Georgia, and Maryland, though the legislative results weren't identical to the governor's recommendations. Going to the legislature hasn't been successful in other states. In California, Maine, and New York, governors and legislative leaders have been unable to agree on actions to bring the current budget into balance. The passage of time without action is particularly critical in New York where the fiscal year ends in March. The consequences have been noticeable. California has lost its Standard & Poor's AAA bond rating. Governor Cuomo attributed his decision not to run for President to inability to reach agreement with legislative leaders on budget-balancing measures.

Things Are Worse Than They Seem

Current shortfalls are more serious than information available to the public shows. There is always a lag between economic events, such as job loss, and their reflection in state revenues. There are also lags between tax collections and reporting of collections and between reporting of collections and revisions of revenue estimates. In addition, new revenue and spending estimates are not announced from October through December in many states. Instead, they are part of budgets released in January.

Sneaky Bad News In Recession: In persistent recession conditions, obscure features of tax systems and spending patterns compound bad news and often deliver it at awkward times. When a worker is out of a job for a quarter of the year, the loss of state income tax revenue is much more than one-fourth. The untaxed portion of income represented by personal exemptions and deductions remains unchanged, so the entire loss affects the taxed portion of income. The effect is exaggerated in states with graduated rates. Recession disproportionately affects corporate profits, with effects on state revenue greatly amplified by loss carryforwards and carrybacks. Property tax delinquency increases which in some states enters school aid formulas to reduce required local tax effort and increase the state aid entitlement.

The statistics that are known on national economic performance and tax collections, and budget estimates in states where they are made in December, all suggest more bad news is on the way.

More Bad News For Next Year

The history of post-World War II recessions suggests that this one should be about over. But economists have proven no more apt at predicting recovery than at predicting recession, with a historical tendency to miss both turning points. This pattern may well be repeated in the revenue estimates for the FY 1993 budgets in most states. This would mean a dim outlook for FY 1993 standing alone and an even dimmer one as the problems of FY 1992 roll into FY 1993. The problems are seen in the form of low or negative balances, unpaid bills, and one time balancing devices that must be replaced with real revenues or spending cuts in the following year.

Nationwide, state tax cuts aren't in the cards. The exceptions are likely to be minor adjustments in the name of economic development, such as expanding enterprise zones, and lowering one tax by increasing another.

In the incremental world of budgeting, *increases* will be a No-No. So the pressures will be strong to avoid increases in: (1) employee pay, (2) outlays for non-cash compensation such as the employer share of health insurance costs, (3) welfare cash payments, (4) school aid, (5) general local aid, (6) reimbursement rates for health care providers, and (7) all other reimbursement rates such as those for foster parents, local jails that take state prisoners, day care, home health care, and social services. Increases in agency budgets for any reason will come under more than the usual scrutiny. New Initiatives will also be a No-No.

The Budget Outlook

In most states, the outlook is for no costly new initiatives in the new FY 1993 budgets. For schools, this means inflation adjustments at best, with new education quality moves confined to those involving little cost such as school governance reforms and student testing. Past legislation calling for more than this may not be funded. For higher education, this means another year, like FY 1992 (Issue 23), with state support below or at inflation.

For welfare, it means little or no increase in payment levels. For welfare and Medicaid, it means no increase in eligibility except as required by federal law. For corrections, it means current service funding in some states and attempts to reduce growth in inmate populations by alternative sentencing and early release in others. For local aid, it means no new programs and some pressure to cut existing ones. For all other programs, it means current service funding, often adjusted by small across-the-board percentage cuts.

Job Growth, 9/90-91	
Nebraska	5.31%
South Dakota	3.06
Utah	3.03
Arkansas	2.78
North Dakota	2.35
Idaho	1.95
Montana	1.91
Arizona	1.50
Colorado	1.44
Hawaii	1.38
Oregon	1.38
New Mexico	1.21
Louisiana	1.20
Wyoming	1.06
Texas	1.05
Kansas	0.82
Mississippi	0.73
Nevada	0.64
West Virginia	0.60
Alaska	0.56
Kentucky	0.51
Illinois	0.43
Minnesota	0.42
Oklahoma	0.40
Iowa	0.31
Washington	0.23
Wisconsin	0.20
Ohio	0.12
South Carolina	-0.07
Indiana	-0.11
North Carolina	-0.65
California	-0.66
United States	**-0.68**
Tennessee	-0.69
Alabama	-0.77
Missouri	-0.78
Pennsylvania	-0.92
Delaware	-1.21
Florida	-1.25
Virginia	-1.38
Maryland	-1.54
Michigan	-1.83
Georgia	-1.89
Vermont	-2.74
New Jersey	-2.84
Connecticut	-2.88
Rhode Island	-3.15
New York	-3.36
Maine	-3.80
New Hampshire	-4.75
Massachusetts	-5.14

Prospects for major tax relief are dim. Less costly relief measures will be considered. Examples are industrial development incentives, business research and development and investment credits, and attempts to lower taxes of low-income wage earners. Some of these could be adopted, but not many. Election-oriented legislators will offer many more costly relief measures -- a penny less sales tax, new sales tax exemptions, new income tax credits -- but these are likely to end their legislative careers in committee.

There will be exceptions. Some states, such as Kansas and Tennessee, may increase taxes enough to fund new initiatives just as Pennsylvania did this year. Litigation on school finance could force action in some states.

States Bucking The Trend?

Will there be exceptions because some state economies are performing well despite recession? Probably not. At the left, states are listed in the order of the percentage gain in jobs from September of 1990 to September of 1991. The top of the page is the logical place to look for states that might buck a national pattern of cutbacks and tax increases. Most of these states have special fiscal problems of one kind or another.

Nebraska (#1) must do something about its property taxes, which have been bouncing around in litigation for several years. An overhaul could require state money to cushion the transition. In South Dakota (#2), the news is that the governor won't press a previously proposed sales tax increase and that income tax proponents aren't likely to be successful. Utah (#3) needs its revenue growth to match growth in education enrollments. Arkansas (#4) just raised taxes for schools, has a revenue shortfall, and has curtailed Medicaid optional services to control cost escalation. Both North Dakota (#5) and Colorado (#9) had special legislative sessions late in 1991. Both deferred discussion of tax hikes until this year.

There are similar stories for states farther down the list. Revenue shortfalls have appeared in Arizona, Montana, Wyoming and many other states in the top half of the list.

THE PERPETUAL FISCAL CRISIS?

> *Forecasts for the future are sobering. Revenue growth will be slow; spending, particularly for health care and prison construction, will continue to explode. Yet, citizens will oppose tax increases. While governors want to expand spending in education, training, and infrastructure investment, their hands will be tied by fiscal reality.*
>
> *The most likely prospect is for a series of tight budgets. Medicaid spending will continue to consume a big share of revenue increases, with federal mandates piled on top of large cost increases resulting from rapid inflation in medical prices as well as greater numbers of senior citizens requiring long-term care. Unless present "get tough" sentencing policies are changed, corrections budgets will also grow rapidly. After paying for increased spending on elementary-secondary schools, state budgets will not have much left over for other programs.*

These glum views of the outlook for state finance reflects what might be called the orthodox perspective on state finances in the 1990s. The statements were published by the major organizations of state officials. The first, by the National Governors' Association in its Governors' Weekly Bulletin (12/13); the second, by the National Association of State Legislatures in a book, The State Fiscal Agenda For The 1990s (1990). Both authors have intimate ties to their publisher. Raymond Scheppach is NGA's executive director and Steven Gold was on NCSL's staff while the book was written.

Summary Of The Theory

The theory is that in the 1990s states will not enjoy as favorable a situation as in the 1980s. Revenue growth will be slower because economic growth won't be as great and because revenue structures won't let states capture the growth that does occur. For example, goods-based sales taxes won't grow as fast as an economy increasingly oriented toward services. Spending growth will be dictated by uncontrollable, or nearly uncontrollable, factors such as school enrollment, corrections, and especially health care. Tax increases won't be an easy solution because voters, subject to the same economic squeeze as states, won't easily surrender additional purchasing power to governments.

State Versions Of The Theory

The same fiscal pessimism has appeared in individual states. The most recent manifestation is California's Growing Taxpayer Squeeze recently released by the governor. Its assessment that there is a mismatch between state spending and revenues is generally accepted by California decisionmakers. From it, the governor concludes that factors that automatically increase spending, such as cost-of-living increases for welfare recipients, must be curbed. Others conclude that taxes must be increased again.

The mismatch is particularly striking in California because of some relatively unique features of both the state's demographics and its tax system. Unlike those of most states, the income tax is indexed for inflation, so there is no fiscal dividend as taxpayers move into higher brackets of the graduated income tax. Because property taxes are constrained by Proposition 13, inflation in property values doesn't translate into automatic increases in local revenue. Spending growth is largely automatic. Proposition 98 guarantees adjustments for inflation and the substantial enrollment growth for both community colleges and public schools. Other laws, some now suspended, guaranteed inflation adjustments for welfare and other entitlements.

A long-term mismatch also appears in California's Commission on State Finance study, 1991 Annual Long-Term General Fund Forecast. Besides identifying a current shortfall, the report projects deficits throughout the 1990s. At the end of the decade, it predicts that spending for current programs will be growing about 8.3% a year while revenues grow at 7.6%.

In other states, projections of spending and revenues show a structural deficit. These can readily be shown in states with fast-growing population and revenue sources that don't respond well to inflation and economic growth. Nevada is a good example. In many Eastern states, there isn't the same demographic pressure on school spending and infrastructure. But there are other problems, such as the demands an aging population creates for Medicaid nursing home payments and needs for infrastructure maintenance.

Implications Of The Theory

The theory has major implications for: (1) tax policy, (2) spending policy and state management, (3) health care, and (4) state approaches to federal policy.

Tax Policy

Part of the problem, as Scheppach puts it, is, "Not only will economic growth be down, but state tax revenues will not keep pace." One solution stressed by Gold is increasing the "elasticity" of state and local tax systems, that is, the responsiveness of tax collections to economic growth. There are several ways to do this. First, eliminating exemptions for the fastest growing portions of a tax base, such as retirement income in the income tax and services in the sales tax. Second, using features that cause revenues to rise faster than income such as a graduated income tax or a flat tax with generous personal exemptions and deductions. Third, basing taxes on value -- like the insurance premiums and public utility taxes -- not physical quantities like gasoline taxes.

Spending Policy And State Management

If needs are expanding more rapidly than revenue and revenue-raising is limited by taxpayer resistance, "more bang for the buck" is the answer. Gold devotes a chapter to increasing accountability, targeting benefits more precisely to those who need them, and what he calls increasing reliance on market mechanisms such as vouchers, decentralization, and privatization. Scheppach talks of more clearly defining priorities, improving effectiveness and efficiency, downsizing, a more entrepreneurial approach to government, more contracting out, quality enhancement, service integration, and more decentralized decisionmaking in return for improved results.

Health Care

Scheppach calls health care reform "the nation's number one domestic priority." He blames uncontrollable health care costs for a significant portion of the fiscal crisis at all levels of government and sees them as limiting the resources that can be put into education, infrastructure, and other public investments. He sees entitlements and mandatory spending, such as many health care programs, as the source of many of the federal government's budget ills and suggests "states are moving toward a similar position." Gold notes that a federal initiative in health care is more likely to add to state costs than reduce them.

Approaches to Federal Policy

One potential solution to a fiscal crisis at the state and local level in the 1990s is to shift some cost to the federal government. Opinions differ on whether it would be appropriate to handle such costs at the federal level. Given other federal commitments but considering reduced needs for defense spending, opinions also differ on whether the federal government could afford to absorb such cost shifts.

The areas of possible federal takeover are unlimited, but several have been stressed by state and local officials in the past: (1) cash welfare including nationally uniform floor levels for those under 65 comparable to those provided for aged and disabled under SSI, (2) indigent medical care, particularly long-term (mostly nursing home) care now provided through Medicaid, and (3) responsibility for special populations such as immigrants. These possibilities aren't pushed by either Gold or Scheppach, but Scheppach sees a different climate in the 1990s for dealing with federal aid cuts and mandates. He describes state finances in the 1980s as "almost too good to be true" and comments:

> *In this growth environment, governors were philosophical about cuts in federal aid to states and other shifts in responsibilities. (During this period, federal aid dropped from 17% to 11% of the states' own tax revenues and the federal government began to tap into state coffers to expand the Medicaid program.)*

> *Voices were raised in opposition. But overall, governors believed the federal deficit was huge and that the states had to accept their share of the budget cuts and take on responsibilities previously met by other levels of government.*
>
> *But the key was that states had the money during the 1980s to accommodate these shifts.*

Implications Of A Perpetual Fiscal Crisis

If there is a perpetual fiscal crisis, there are some significant implications for state policy and for those activities most affected by state funding levels.

One is that multi-year state plans that assume finances will be in better shape in the future aren't appropriate because they can lead to stop and start funding, poor planning, and wasted resources. One example is the multi-year school aid and educational quality plans. Mississippi adopted one, but then didn't fund even the first year. Georgia and other states have consistently decided that their appetite for school spending was higher in passing an education bill with out-year funding than an appropriations bill with budget year funding. Colorado's legislature recently met to scale back a previously adopted school program.

Education isn't the only example. Some states such as Michigan have built prisons but then delayed opening because they didn't have operating money. California and Massachusetts adopted extensive bond-funded programs for many purposes in the 1980s, but now are curtailing them and avoiding new ones. The results of a curtailed large program and of a program designed to be smaller aren't necessarily the same. For example, school construction was squeezed in California by the stop and start process -- getting less than it would have if a smaller lower ceiling for bond issuance had been chosen.

Another implication of perpetual fiscal crisis is that pressures will probably continue for financing a higher percentage of some current costs by fees. In at least two cases, this assumption affects management and spending patterns in major ways. The first is parks, where a higher fee policy will affect what parks are used how much and what types of facilities are most used. In higher education, a continuation of the tuition increases in the past several years will have major effects on enrollment, reducing the need for additional construction in many circumstances and limiting the feasibility of new academic programs because the competition for students will be stiffer.

If there is a perpetual fiscal crisis in state and local government, there will be no room for expensive new initiatives without major tax increases to fund them. This would mean that universal health care plans, major state housing programs, and other proposals for state action would have limited prospects for adoption.

STICKING IT TO THE POOR

> *State budget cuts aimed at the poorest of the poor were so extensive in 1991 and loom so large next year that states seem to be "competing to make themselves unattractive places for the poor to live," a state budget analyst said yesterday.*

This line began the Washington Post's (12/19) description of materials presented by the Center on Budget and Policy Priorities on how recent state budget decisions have impacted the poor. The major conclusion is that the poor were hit hard in many states by decisions on spending -- cash assistance, housing, and other programs -- and by increases in taxes that were often regressive.

Were The Poor Singled Out For Cuts?

The report doesn't take a position on whether, on balance, the poor were hurt more than other groups, indicating data aren't available for such an analysis. It did state that the poor "shouldered a larger share of deficit reduction than other groups in some identifiable respects." One was where regressive taxes, such as a sales tax increase, were used to close budget gaps. The other was that welfare recipients who had benefits cut "are almost certain to have lost a larger share of their income than any other group." This is certainly true except for the small number of persons who lost all their income because they lost their state jobs.

Comparing dollars spent by states in FY 1991 to dollars likely to be spent in FY 1992, the poor most certainly are doing better than other income groups. The big dollar increases in state spending will be in income-tested AFDC and Medicaid because of caseload increases and health care price and utilization increases. Two other gainers in many states, elementary and secondary education and corrections, aren't targeted at the poor, but aren't targeted at other income groups either.

Comparing dollars to be spent in FY 1992 against current service spending levels would be difficult, but would probably show elementary and secondary education doing somewhat better than programs explicitly targeted to the poor. Any method of comparison would show higher education the big loser in the budget decisions of FY 1991 and FY 1992.

The Center's report points out that some states made decisions, like cutting general assistance and AFDC benefit levels and raising sales rather than income taxes, that other states didn't make. From this, it concludes that states didn't need to impact the poor as much as they did. This conclusion is clearly true about programs for the poor, programs for the arts, higher education, or any other single program. In every case, some states will have treated the program of interest more favorably than the average state.

Funding Cash AFDC Benefits

The Center surveyed the states to determine changes in maximum AFDC benefit levels. Only 11 states increased benefits. They were nine states in the West plus Alabama and Florida. Most states left benefits unchanged, and thus with reduced purchasing power. Four states reduced benefits: Michigan by 12.6%, Maryland by 7.1%, Tennessee by 5.1%, and California by 5.1%.

There continue to be striking disparities among the states in the levels of welfare benefits provided under the AFDC program. The maximum benefits, as shown in Table 1, are over $600 a month in five states and over $500 a month in a dozen states. But no family gets over $200 a month in five states or over $300 a month in thirteen states.

Table 1: Maximum Monthly AFDC Payment, January of 1992

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Alaska	$924	18	Kansas	$422	35	New Mexico	$324
2	Connecticut	680	19	Pennsylvania	421	36	Idaho	317
3	Vermont	673	20	South Dakota	404	37	Florida	303
4	Hawaii	666	21	Utah	402	38	Missouri	292
5	California	663	22	North Dakota	401	39	Indiana	288
6	New York	577	23	Montana	390	40	Georgia	280
7	Rhode Island	554	24	Maryland	377	41	North Carolina	272
8	Massachusetts	539	25	Nevada	372	42	West Virginia	249
9	Minnesota	532	26	Illinois	367	43	Kentucky	228
10	Washington	531	27	Nebraska	364	44	South Carolina	210
11	Wisconsin	517	28	Wyoming	360	45	Arkansas	204
12	New Hampshire	516	29	Colorado	356	46	Louisiana	190
13	Oregon	460	30	Virginia	354	47	Tennessee	185
14	Michigan	459	31	Oklahoma	341	48	Texas	184
15	Maine	453	32	Delaware	338	49	Alabama	149
16	Iowa	426	33	Arizona	334	50	Mississippi	120
17	New Jersey	424	34	Ohio	334			

The interaction of AFDC payment levels with eligibility for AFDC and Medicaid payments is complex. Through it, the Center estimates that some families will be forced out of AFDC and Medicaid eligibility as a result of the changes in Maine, Maryland, Michigan, and Vermont.

More benefit cuts may be in the offing. They are under discussion in Tennessee if no tax package is adopted. Governor Wilson is pushing an initiative for the November 1992 ballot in California that would cut AFDC 10% across the board and make deeper cuts in some circumstances.

Benefit cuts could become an issue in many of the states in the first column of Table 1. Many of them are also states where major fiscal problems are expected in the FY 1993 budget at a time when elected officials aren't amenable to increasing taxes.

Funding Other Benefits

In most states, the cash assistance amounts shown in Table 1 understate the income support provided because of special help called special needs payments and emergency assistance. These deal with extraordinary costs (e.g., burial expenses), adverse circumstances (e.g., eviction, utility cutoff), and other case-by-case needs associated with high utility bills, special clothing needs, and other circumstances. Not all states provide special allowances for such circumstances. Some that do cut back their programs this year. Examples include California, Massachusetts, and Michigan. Some states have had energy assistance programs over and above the federal program. Connecticut and Illinois eliminated their programs in the 1991 budget action while Kansas scaled back its program.

State-funded general assistance programs were eliminated or curtailed in Arizona, Connecticut, Illinois, Kansas, Maine, Maryland, Massachusetts, Michigan, Minnesota, New Mexico, New York, Ohio, and Washington. The Center calculates that these cuts will affect half a million people, more than a third of all general assistance recipients nationwide. Many of these recipients will simultaneously lose their eligibility for state-funded health benefits outside the Medicaid program.

The federal government assumed responsibility for cash assistance to the aged, blind, and disabled with the Supplemental Security Income (SSI) program adopted in the 1970s. The benefit is uniform nationally. For someone without other income, it will be $422 a month throughout 1992, $633 a month for a couple. When the national benefit standard was adopted, some states opted to supplement the federal payment while other states did not. The pattern since has differed dramatically. A few states have consistently increased their supplements. Others have maintained them at about the original level. In FY 1992, Alaska will supplement the individual benefit by $362 a month, followed by Connecticut ($325), California ($223), and Massachusetts ($129). Supplements between $50 and $100 are provided by Colorado, Idaho, Minnesota, New York, Oklahoma, Rhode Island, Vermont, and Wisconsin.

Supplements for FY 1992 were left unchanged in most states that use them. Reductions were made in Connecticut, Michigan, Utah, and Wisconsin. Alaska adjusted benefits upward for inflation while Colorado and Nebraska adopted increases that in effect rescinded some of the cuts made last year.

State Housing Programs

Housing subsidies have traditionally been provided directly by the federal government and through federal programs administered by local housing authorities, the entities that own and operate public housing units. With a few exceptions, particularly New York, state involvement was minimal except for the use of tax-exempt bond financing by state housing authorities.

Over the past decade, there has been an effort by federal officials and housing advocates to involve state governments more in housing finance. The result has been mixed. In FY 1992, the Center's survey identifies $1,391 million in state housing finance activities, as shown in Table 2. The table doesn't count the self-liquidating mortgage loans financed with tax exempt bonds, but does count housing financed with general obligation bonds.

Table 2: Housing Program Funding In FY 1992 ($ millions)

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	New York	$390.7	12	Hawaii	$10.6	23	New Hampshire	$2.4
2	Massachusetts	257.4	13	Illinois	10.1	24	West Virginia	2.0
3	California	241.7	14	Texas	9.0	25	Arizona	1.9
4	Connecticut	112.3	15	Oregon	8.4	26	Rhode Island	1.5
5	New Jersey	90.5	16	Alaska	8.1	27	Delaware	1.3
6	Maryland	52.1	17	Ohio	7.0	28	New Mexico	1.3
7	Pennsylvania	30.9	18	Wisconsin	6.7	29	Utah	1.2
8	Washington	24.0	19	Vermont	6.6	30	Maine	1.0
9	Minnesota	16.8	20	Virginia	5.1	31	Colorado	0.6
10	Michigan	16.0	21	Iowa	4.0	32	Oklahoma	0.4
11	Florida	13.4	22	Georgia	3.4	33	Indiana	0.2

State participation varies substantially. The 17 states not shown have no programs. Another eleven states are spending less than $2.5 million or enough to finance about 50 houses a year. The top five states account for $1.1 billion or over three-fourths of the national total.

State fiscal circumstances are having an impact on these programs. FY 1992 spending for emergency programs for the homeless is down $41 million or 7% and spending for "affordable housing" programs is down $246 million or 22%.

The Outlook For State Programs For The Poor

In the tight budget environment predicted for major states over the next year, no one expects the poor to fare very well. The Center's report urges that state officials shield the poor. It cites Pennsylvania, Texas, and Vermont as states that did this. They made small or no cuts in safety net programs for the poor. Pennsylvania and Vermont accompanied their tax increases with tax cuts for some poor households.

Eight states were singled out as taking the harshest actions in 1991, with Massachusetts and Michigan the prime examples. Not surprisingly, the states with the best treatment of the poor by the Center's reckoning were substantial raisers of taxes, while those with the harshest treatment raised taxes less or not at all. It wouldn't be surprising to see this pattern repeated in 1992. State officials determined not to raise taxes will find cuts in welfare and safety net programs appropriate, while those determined to protect the purchasing power of those programs will find tax increases appropriate.

Steven Gold (Center for the Study of the States) who collaborated on the Center's study testified in December before a subcommittee of the U.S. House Ways and Means Committee on state policies and the poor. He concluded:

> *State cutbacks -- concentrated, as they are, in the states with relatively generous safety nets -- confirm the wisdom of those who call for assumption of welfare costs by the federal government. We could be entering a period in which states increasingly compete to make themselves unattractive places for the poor to reside.*

SPENDING AND TAX LEVELS

New State Comparisons Of Taxes And Spending

The Census Bureau recently published the fiscal information that it alone has the resources to gather -- complete data on roughly 80,000 state and local governments for FY 1990. Again this year, it didn't make the key calculations required for comparisons among states, which **Reports** has done for this article. Also included are calculations of balance in state tax systems that rely on Census data, but are never prepared by the Census Bureau.

Interstate comparisons of state governments alone, or local governments alone, aren't useful for policymaking purposes. The diversity of state-local division of responsibility makes such comparisons meaningless. The State of New Hampshire, which has almost no state school aid, spends much less on schools than the average state, which pays about half of local school costs. New York makes its local governments pay a large part of welfare and Medicaid costs; most states don't. Comparisons of state spending alone are useful as debaters' points in campaigns as states which assume many responsibilities spend much more than states that don't. All comparisons in this article combine state and local spending and taxes.

State And Local Taxes Per Capita

The latest per capita tax comparisons, which will remain current until about this time next year, are shown in Table 3.

Table 3: State And Local General Taxes Per Capita, 1990

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Alaska	$4,069	17	Vermont	$2,012	34	North Carolina	$1,675
2	New York	3,267	18	Maine	1,974	35	Texas	1,662
3	Connecticut	2,674	19	Oregon	1,934	36	Indiana	1,631
4	Hawaii	2,596	20	Nevada	1,928	37	Utah	1,582
5	New Jersey	2,527	21	Colorado	1,925	38	Oklahoma	1,575
6	Minnesota	2,463	22	Arizona	1,921	39	North Dakota	1,569
7	Massachusetts	2,359	23	Virginia	1,896	40	West Virginia	1,562
8	Maryland	2,305	24	Iowa	1,881	41	South Carolina	1,562
9	California	2,220	25	Pennsylvania	1,859	42	Louisiana	1,562
10	Wyoming	2,209	26	Kansas	1,847	43	Idaho	1,561
11	Washington	2,123	27	Ohio	1,813	44	Missouri	1,552
	United States	**2,016**	28	Nebraska	1,803	45	Kentucky	1,496
12	Illinois	2,102	29	Georgia	1,801	46	South Dakota	1,447
13	Wisconsin	2,090	30	Montana	1,795	47	Tennessee	1,399
14	Michigan	2,068	31	Florida	1,746	48	Alabama	1,328
15	Delaware	2,056	32	New Hampshire	1,693	49	Arkansas	1,273
16	Rhode Island	2,037	33	New Mexico	1,690	50	Mississippi	1,264

The states with the highest per capita incomes tend to have the highest rankings in per capita taxes. Because changes in population and state and local revenues are relatively slow, the rankings tend to be stable from year to year. Among the top ten states, Hawaii moved from fifth to fourth, switching places with New Jersey but reversing the switch the two states made last year. Minnesota moved from eight to sixth knocking Massachusetts and Maryland down a rank. Wisconsin moved from thirteenth to tenth shifting Wyoming out of the top ten. There was no change in the bottom five states.

State And Local Taxes In Relation To Personal Income

Although there are widespread concerns about the rising burden of state and local taxes, the revenues from those taxes as a percentage of personal income has been stable. In FY 1990, they took 11.52% of income, off slightly from the 11.56% taken in FY 1989 and FY 1988. This percentage should move sharply upward for FY 1991 and FY 1992. Recession cuts the growth in personal income. It also affects tax collections but not as much because property taxes are largely unaffected and many state and local governments increased tax rates.

Many users prefer comparisons to personal income to per capita comparisons. The personal income comparisons are shown in Table 4.

Table 4: State And Local Taxes as Percent Of Personal Income, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Alaska	19.62%	18	Louisiana	11.64%	34	Oklahoma	10.85%
2	New York	15.54		**United States**	**11.52**	35	Nevada	10.83
3	Wyoming	14.57	19	Nebraska	11.43	36	Massachusetts	10.82
4	Minnesota	14.02	20	California	11.41	37	Kentucky	10.76
5	Hawaii	14.00	21	Rhode Island	11.40	38	Pennsylvania	10.62
6	Wisconsin	12.77	22	South Carolina	11.38	39	New Jersey	10.62
7	New Mexico	12.75	23	Idaho	11.31	40	Texas	10.58
8	Montana	12.64	24	Georgia	11.29	41	Mississippi	10.58
9	Arizona	12.53	25	North Dakota	11.20	42	South Dakota	10.29
10	Washington	12.30	26	Maryland	11.18	43	Indiana	10.25
11	Oregon	12.24	27	North Carolina	11.12	44	Virginia	10.16
12	West Virginia	12.22	28	Kansas	11.04	45	Florida	10.10
13	Utah	12.21	29	Ohio	11.01	46	Arkansas	9.64
14	Maine	12.21	30	Delaware	11.01	47	Alabama	9.56
15	Vermont	12.21	31	Connecticut	11.00	48	Missouri	9.45
16	Michigan	11.88	32	Illinois	10.95	49	Tennessee	9.40
17	Iowa	11.88	33	Colorado	10.89	50	New Hampshire	8.37

Several of the states with high taxes in relation to personal income are getting their revenue from the personal income of residents of other states. Taxes on oil and gas by Alaska (#1), on oil, gas, and coal by Wyoming (#3), and on tourists by Hawaii (#5) are examples. The other states shown with high taxes are simply taxing their resident individuals and businesses much more than other states. By this measure, New York's taxes are 35% higher than the national average and Minnesota's are 22% above average.

The state rankings are little changed from last year. The top three ranks are unchanged while Minnesota took fourth from Hawaii, dropping it to fifth. In the bottom six ranks, the only change was that Tennessee gave 48th to Missouri and took its former rank of 49th. There are more changes in the middle ranks, primarily reflecting movement in personal income (the denominator) rather than taxes (the numerator). New England's rapid growth was continuing through CY 1989, the year of the personal income data Census uses for this comparison. As a result, Maine moved from fifth two years ago to sixth last year to 14th this year. Massachusetts moved from 22nd to 28th to 36th. These states will soar in rankings next year and in the year following because they have raised taxes while their personal income growth has trailed the rest of the nation.

Property Tax Burdens

Table 5 expresses property taxes as a percentage of personal income. The U. S. average of 3.58% is slightly up from the 3.52% in FY 1989.

Table 5: State And Local Property Taxes As A Percent Of Personal Income, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Alaska	6.01%	18	Texas	4.14%	34	Pennsylvania	2.95%
2	Wyoming	5.98	19	Minnesota	4.03	35	South Carolina	2.92
3	Montana	5.83	20	Kansas	3.93	36	Maryland	2.86
4	New Hampshire	5.70	21	Illinois	3.93	37	Mississippi	2.85
5	Oregon	5.40	22	Colorado	3.87	38	Nevada	2.38
6	Vermont	5.01		**United States**	**3.58**	39	North Carolina	2.34
7	New York	4.87	23	Massachusetts	3.56	40	Tennessee	2.16
8	New Jersey	4.86	24	Florida	3.54	41	Missouri	2.08
9	Nebraska	4.76	25	North Dakota	3.41	42	Hawaii	2.07
10	Michigan	4.71	26	Washington	3.38	43	West Virginia	2.01
11	Wisconsin	4.51	27	Utah	3.33	44	Louisiana	2.00
12	Rhode Island	4.51	28	Virginia	3.20	45	Oklahoma	1.91
13	Maine	4.46	29	Ohio	3.13	46	Kentucky	1.82
14	Connecticut	4.34	30	California	3.11	47	Arkansas	1.73
15	Iowa	4.17	31	Georgia	3.10	48	New Mexico	1.65
16	South Dakota	4.15	32	Idaho	3.01	49	Delaware	1.62
17	Arizona	4.15	33	Indiana	2.97	50	Alabama	1.17

The top three states owe their position primarily to taxing resource wealth, not individuals and commercial activities. The other top states have high property taxes because they don't use other taxes (e.g., sales and income in New Hampshire, sales in Oregon) or have generally high taxes and spending like New York and Vermont.

The level of burden in these states is high enough to have considerable impact on state policy. Since the year covered by these data: (1) New Hampshire has come closer than ever to enacting an income tax, (2) Oregon voters approved an initiative to roll back property taxes and force the state to replace the lost revenue, (3) Vermont legislators opted for a major tax increase this year rather than following other New England states in cutting local aid sharply, (4) Nebraska and New Jersey raised income and sales taxes to lower property taxes, (5) Michigan set new limits on property taxes after a ballot measure to raise sales taxes to lower property taxes was rejected by voters, and (6) Wisconsin counties have been adopting a new local option sales tax.

Sales Tax Burdens

Sales tax collections of state and local government are shown in Table 6. A broad definition of sales taxes was used to develop the table. It includes regular sales and use taxes plus special excise taxes on commodities such as tobacco and services such as public utilities.

Table 6: State And Local Sales Taxes As Percent Of Personal Income, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Washington	7.66%	18	Arkansas	4.51%	34	Nebraska	3.77%
2	Hawaii	7.57	19	North Dakota	4.43	35	Kansas	3.76
3	Nevada	6.96	20	Connecticut	4.35	36	Rhode Island	3.60
4	New Mexico	6.75	21	New York	4.15	37	Ohio	3.55
5	Louisiana	5.94	22	Missouri	4.11	38	Iowa	3.46
6	Tennessee	5.71	23	North Carolina	4.11	39	Vermont	3.46
7	Arizona	5.51		**United States**	**4.08**	40	Pennsylvania	3.18
8	Florida	5.33	24	Idaho	4.06	41	Virginia	3.10
9	West Virginia	5.30	25	Illinois	4.06	42	New Jersey	2.96
10	Texas	5.27	26	Kentucky	4.02	43	Maryland	2.92
11	Mississippi	5.20	27	Minnesota	3.97	44	Michigan	2.76
12	Utah	4.96	28	Colorado	3.90	45	Massachusetts	2.21
13	South Dakota	4.93	29	Maine	3.89	46	Montana	1.61
14	Alabama	4.82	30	Indiana	3.85	47	Alaska	1.56
15	Oklahoma	4.66	31	Wyoming	3.83	48	Delaware	1.29
16	Georgia	4.56	32	California	3.82	49	New Hampshire	1.21
17	South Carolina	4.53	33	Wisconsin	3.80	50	Oregon	1.09

With their ability to collect sales taxes from the personal income of other states by taxing tourists, Hawaii and Nevada rank high in this measure. So do states that have no income tax like Washington, Nevada, Tennessee, and Florida. The five states at the bottom of the list have no general sales tax.

The aggregate sales tax burden of 4.08% of personal income is little changed from 4.10% the prior year. By moving its burden from 7.37% of income to 7.66%, Washington took the top spot held last year by Hawaii. Also by tax increases, West Virginia moved from 18th last year to ninth. Over the next several years, there will be major reshuffling of ranks in the middle of this table because some states have increased sales tax rates and some haven't. Local option taxes should raise the burdens in South Carolina, Wisconsin, and a few other states. State increases will raise the burdens in New Jersey, Pennsylvania, and other states. Connecticut should drop because some of its new income tax revenue is being used to lower the sales tax.

Individual Income Tax Burdens

The use of personal income taxes continues to show wide differences in state tax policy that are reflected in Table 7.

Table 7: State And Local Personal Income Taxes As Percent Of Personal Income, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	New York	4.72%	18	Georgia	2.78%	34	Illinois	1.95%
2	Maryland	4.30	19	Vermont	2.70	35	Arizona	1.89
3	Oregon	4.07	20	Virginia	2.67	36	New Mexico	1.80
4	Delaware	3.86	21	Michigan	2.67	37	New Jersey	1.60
5	Massachusetts	3.74	22	Indiana	2.65	38	Mississippi	1.40
6	Minnesota	3.74	23	Montana	2.47	39	Louisiana	1.30
7	North Carolina	3.39	24	Pennsylvania	2.46	40	North Dakota	1.18
8	Hawaii	3.38		**United States**	**2.43**	41	Connecticut	0.76
9	Ohio	3.32	25	Arkansas	2.38	42	New Hampshire	0.18
10	Wisconsin	3.28	26	Rhode Island	2.38	43	Tennessee	0.14
11	Kentucky	3.03	27	Missouri	2.38		South Dakota	0.00
12	Maine	2.92	28	Colorado	2.31		Texas	0.00
13	California	2.90	29	West Virginia	2.25		Alaska	0.00
14	Idaho	2.90	30	Oklahoma	2.19		Florida	0.00
15	Utah	2.90	31	Alabama	2.09		Nevada	0.00
16	Iowa	2.90	32	Kansas	2.07		Washington	0.00
17	South Carolina	2.88	33	Nebraska	1.99		Wyoming	0.00

Seven states have nothing resembling a personal income tax. In FY 1990, three others -- Connecticut, New Hampshire, and Tennessee -- reached only a limited portion of income such as interest, dividends, and capital gains. While these ten states tap less than 1% of personal income, eleven states tax more than 3% of all personal income.

From FY 1989 to FY 1990 there were few changes in this table. The national average burden moved marginally up from 2.41% to 2.43%. The top ranks remained unchanged except that Hawaii reduced its taxes and dropped from fourth to eighth, moving other states up a rank.

Bigger changes will appear in future years. Connecticut's new income tax and tax increases in Arizona, Illinois, and New Jersey should move those states out of the bottom third. Increases in Pennsylvania, Rhode Island, Oklahoma, and Nebraska will move those states up as well.

BALANCE IN STATE TAX SYSTEMS

Some experts on state tax systems urge state officials to keep their systems "balanced." The concept is roughly equal reliance on each of the "big three" taxes -- property, sales, and income. Table 8 provides a basis for assessing how well states have been doing this. It shows revenues raised by each of the big three as a percentage of the total revenues raised by all three.

Table 8: Percentage Of State And Local Tax Revenue Of Major Tax Revenues Raised From Each Of The Major Taxes, 1990

State	Property	Sales	Income	State	Property	Sales	Income
Alabama	15%	60%	26%	Nebraska	45%	36%	19%
Alaska	79	21	0	Nevada	25	75	0
Arizona	36	48	16	New Hampshire	80	17	3
Arkansas	20	52	28	New Jersey	52	31	17
California	32	39	30	New Mexico	16	66	18
Colorado	38	39	23	New York	35	30	34
Connecticut	46	46	8	North Carolina	24	42	34
Delaware	24	19	57	North Dakota	38	49	13
Florida	40	60	0	Ohio	31	35	33
Georgia	30	44	27	Oklahoma	22	53	25
Hawaii	16	58	26	Oregon	51	10	39
Idaho	30	41	29	Pennsylvania	34	37	29
Illinois	40	41	20	Rhode Island	43	34	23
Indiana	31	41	28	South Carolina	28	44	28
Iowa	40	33	28	South Dakota	45	55	0
Kansas	40	39	21	Tennessee	27	71	2
Kentucky	20	45	34	Texas	44	56	0
Louisiana	22	64	14	Utah	30	44	26
Maine	40	34	26	Vermont	45	31	24
Maryland	28	29	43	Virginia	36	35	30
Massachusetts	37	23	39	Washington	31	69	0
Michigan	46	27	26	West Virginia	21	55	24
Minnesota	34	34	32	Wisconsin	39	33	28
Mississippi	30	55	15	Wyoming	61	39	0
Missouri	24	48	28	**United States**	**35**	**40**	**24**
Montana	59	16	25				

Except in special circumstances, such as Alaska's reliance on taxing oil and gas, there is considerable pressure for states with unbalanced tax systems to change them. Those interested in more spending urge use of the unused or underused tax, as happened with the income tax in Connecticut this year. Those affected by overused taxes, such as property taxpayers in Oregon, also urge change -- not necessarily advocating higher other taxes but advocating reduction in the tax that concerns them.

As a result, major deviations from balance often identify the states where the pressures for tax changes will be greatest. Table 9 shows the states with the highest percentage reliance on individual tax sources (as shown in Table 8). It designates those states where major change has already taken place (*) and where change is now being considered seriously (**).

Table 9: States With High And Low Reliance On Particular Tax Sources, FY 1990

Rank	Property	Sales	Income
1	New Hampshire**	Nevada*	Delaware
2	Alaska	Tennessee**	Maryland**
3	Wyoming	Washington**	Massachusetts**
4	Montana**	New Mexico**	Oregon*
5	New Jersey*	Louisiana**	North Carolina*
6	Oregon*	Florida**	New York
7	Michigan**	Alabama**	Kentucky
8	Connecticut*	Hawaii	Ohio
9	Nebraska*	Texas	Minnesota
10	South Dakota**	West Virginia	Virginia

The table suggests that the agitation for movement toward a more balanced tax system is substantial. The environment for change has been strongest in the high property tax states. There is much less pressure for change in the states with high reliance on individual income taxes, partly because income taxes account for more than 40% of big three tax yield in only the top two states. Sales taxes are over 50% of big three yield in 14 states and property taxes over 40% of big three yield in 13 states.

MISCELLANY

Health Care Reform

> *The more specific I get ... the more I run the risk of having this whole thing fall apart.*

With that comment, Vermont's Governor Dean summed up the problems of state elected officials in dealing with health care. Dean, a doctor, is trying to cope with recommendations of the Governor's Blue Ribbon Commission on Health Care. The commission agreed on goals, such as cost containment and universal access to health services, but little else except creating a state agency to carry on its work. Given the state's fiscal circumstances, the major options being considered for 1992 are those involving regulation of health insurers and providers, not those involving paying for care.

Interacting State And Local Fiscal Problems

As recession continues it becomes harder and harder for local governments and the states to adopt the roles of drowning man and lifeguard. The states can't provide fiscal bailouts if their own finances are in trouble. Nor can they shift their own fiscal problems downward if a significant number of local governments will be in serious trouble as a result. The apt analogy may not be potential drowning victim and rescuer, but two potential drowning victims.

In assessing the situation ("Too Many Needs, Too Little Money," State Legislatures, December), NCSL's fiscal affairs director Ronald Snell notes the recession "has brought a reversal of the decade-long pattern of increasing state aid to local governments." He observes that state aid is different from federal aid, with primary emphasis on education and highways rather than aid for general purposes and infrastructure. Noting that some states, particularly in the Northeast, have recently reduced aid to local government, Snell concludes, "The challenge now is for state and local officials to understand how hard economic times injure all kinds of governments and to find new ways to balance public desires for services against limited public resources."

New York State and New York City have recently been dancing to the same tune, though not exactly as partners. After considerable agony, both adopted balanced FY 1992 budgets with noticeable cuts in current service spending and tax increases. Recently officials of both have announced that their FY 1993 current service budgets are out of balance and that shortfalls are also likely in the current fiscal year. Then within a month of the first announcement, both announced that the problems could be more serious than indicated in the previous announcement.

The gap numbers are large, something like $3-4 billion for the state and upwards of $1.2 billion for the city. The city's problem would be minimized by more state aid. The state's problem would be minimized by less state aid. Similar problems will be found throughout the nation, but are most serious in the Northeast.

Unfunded mandates are a major part of local officials' concerns with how states cause fiscal problems for local government, though defining them and quantifying their impact isn't easy, as NCSL staffer Scott Mackey details in "When Local Business Becomes State Business," (State Legislatures, December).

Urbanization of America

The Census Bureau recently announced that 75.2% of the nation's population is now (1990) urban, up from 73.7% in 1980. The urbanization statistics for each state are shown in Table 10.

Table 10: Percentage Of State Population That Is Urban, 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	California	92.6%	17	Ohio	74.1%	34	Georgia	63.2%
2	New Jersey	89.4	18	Delaware	73.0	35	Tennessee	60.9
3	Hawaii	89.0	19	New Mexico	73.0	36	Iowa	60.6
4	Nevada	88.3	20	Michigan	70.5	37	Alabama	60.4
5	Arizona	87.5	21	Oregon	70.5	38	Idaho	57.4
6	Utah	87.0	22	Minnesota	69.9	39	South Carolina	54.6
7	Rhode Island	86.0	23	Virginia	69.6	40	Arkansas	53.5
8	Florida	84.8	24	Kansas	69.1	41	North Dakota	53.3
9	Illinois	84.6	25	Pennsylvania	68.9	42	Montana	52.5
10	Massachusetts	84.3	26	Missouri	68.7	43	Kentucky	51.8
11	New York	84.3	27	Louisiana	68.1	44	New Hampshire	51.0
12	Colorado	82.4	28	Oklahoma	67.7	45	North Carolina	50.4
13	Maryland	81.3	29	Alaska	67.5	46	South Dakota	50.0
14	Texas	80.3	30	Nebraska	66.1	47	Mississippi	47.1
15	Connecticut	79.1	31	Wisconsin	65.7	48	Maine	44.6
16	Washington	76.4	32	Wyoming	65.0	49	West Virginia	36.1
	United States	**75.2**	33	Indiana	64.9	50	Vermont	32.2

The urban-rural comparison was undoubtedly a more meaningful one before widespread ownership of automobiles. The Census Bureau definition includes persons living in densely populated areas and places of 2,500 more outside urbanized areas. The definition won't necessarily fit with common notions of urban, such as a housing development in an unincorporated area near a central city. The definition can lead to some unexpected results. While the nation became more urban from 1980 to 1990, eleven states became more rural including Michigan, Pennsylvania, and Rhode Island.

College Savings Programs

In the late 1980s, Michigan offered parents and others the opportunity to guarantee payment of tuition costs at state universities by contracts made with the state when the children were young. The concept was that the state would hold the money in the Michigan Education Trust, which would be self supporting because the (assumed) rate of return on investments would be enough higher than the increase in tuition costs to cover the administrative expenses.

The plan was presumed to be preferable to individual parents making the same investments because: (1) the parents would be tempted to spend the money on something else, (2) the state would better be able to purchase a diversified portfolio of investments with low administrative costs, (3) the parents would be protected from lower-than-expected interest rates and higher-than-expected tuition increases, and (4) the interest earnings in the trust wouldn't be taxable while interest would be taxable if the parents held the money. The program has been popular with 55,000 contracts in effect with an average investment of about $8,000. Several states copied the idea.

Many states didn't follow Michigan's lead. Some did nothing. Some issued some of their regular tax-exempt debt issues in small denominations and touted them as appropriate investments for parents seeking to accumulate a nest egg for college costs.

Michigan has now discontinued its program. In part it is a casualty of changing economic circumstances. It was originally assumed that the state could earn nearly 10% on investments and that tuition would rise 7.3% annually, leaving 2.5% spread for administrative costs and reserves. Partly because of restrictions on state appropriations, university tuition has been rising faster than assumed. In the current economic circumstances, interest rates are lower, dropping the expected spread to under 1%. In addition, IRS is pressing its case that the interest earned must be taxable -- to Michigan's fund if not to the parent-taxpayer.

TECHNICAL NOTES

Another Tight Year: NCSL has surveyed legislative fiscal officers to produce NCSL State Budget Update: November 1991 and updated the survey in December. For details on shortfalls, see those documents and State Budget & Tax News coverage of individual states.

Sticking It To The Poor: The report, The States And The Poor: How Budget Decisions In 1991 Affected Low Income People, was published by the Center on Budget and Policy Priorities (777 N. Capitol St., N.E., Washington, DC 20002).

Spending And Tax Levels: The data on spending and taxes come from the Census Bureau's Government Finances: 1989-90, Preliminary Report. The personal income and population data are those used in the Census report, State Government Finances: 1990. The data are for fiscal years ending in 1990, FY 1990 for states and many local governments and CY 1990 for the local governments on a calendar year basis. Following Census practice, personal income is for CY 1990 and the population count is from the 1990 Census.

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VOLUME 10 ISSUE 2

IN THIS ISSUE

Different states face different challenges because of differing demograhics -- how fast population is growing or shrinking, the impact of immigration, whether states are drawing residents from other states, and births of future public school and university students. Developments since the 1990 Census may foretell trends of a decade.

- Population Growth And Change p. 2

As recession continues, over half the states find tax collections running below estimates and at least 35 states have spending running above estimates. Cutting spending is the preferred solution, but there are two lists predicting a substantial number of tax hikes this year. The public's preference is higher spending and lower taxes.

- The Fiscal Outlook p. 9

State officials are looking at ways they can combat recession. Federal leaders are preparing economic stimulus packages, some with new grants for state and local government. Meanwhile, state and local officials are struggling to balance their budgets, which some economists argue has perverse economic effects.

- States And The Recession p. 14

Other articles cover a range of topics including the costs of health care in state budgets, how states compare in birth rates and taxes on affluent families, a lull in use of voter initiatives, whether high payments draw welfare recipients, and two aspects of population statistics.

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STATE POLICY REPORTS

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January 1992 (Second Of Two January Issues)

POPULATION GROWTH AND CHANGE

New Population Statistics

The Census Bureau has released new population estimates. They show the U. S. population (including 598,000 District of Columbia residents) to be 252,177,000 as of July 1, 1991. The state estimates shown in Table 1 are consistent with the 1990 Census. This means they *exclude* five million or so residents arguably missed by the Census count.

Table 1: State Population (000) In 1991
With Cumulative Percentage Of 50-State Total

Rank	State	Number	Cum. Pct.	Rank	State	Number	Cum. Pct.
1	California	30,380	12.1%	26	Colorado	3,377	85.1%
2	New York	18,058	19.3	27	Connecticut	3,291	86.4
3	Texas	17,349	26.1	28	Oklahoma	3,175	87.6
4	Florida	13,277	31.4	29	Oregon	2,922	88.8
5	Pennsylvania	11,961	36.2	30	Iowa	2,795	89.9
6	Illinois	11,543	40.8	31	Mississippi	2,592	90.9
7	Ohio	10,939	45.1	32	Kansas	2,495	91.9
8	Michigan	9,368	48.8	33	Arkansas	2,372	92.9
9	New Jersey	7,760	51.9	34	West Virginia	1,801	93.6
10	North Carolina	6,737	54.6	35	Utah	1,770	94.3
11	Georgia	6,623	57.2	36	Nebraska	1,593	94.9
12	Virginia	6,286	59.7	37	New Mexico	1,548	95.5
13	Massachusetts	5,996	62.1	38	Nevada	1,284	96.0
14	Indiana	5,610	64.3	39	Maine	1,235	96.5
15	Missouri	5,158	66.4	40	Hawaii	1,135	97.0
16	Washington	5,018	68.4	41	New Hampshire	1,105	97.4
17	Wisconsin	4,955	70.4	42	Idaho	1,039	97.8
18	Tennessee	4,953	72.3	43	Rhode Island	1,004	98.2
19	Maryland	4,860	74.3	44	Montana	808	98.6
20	Minnesota	4,432	76.0	45	South Dakota	703	98.8
21	Louisiana	4,252	77.7	46	Delaware	680	99.1
22	Alabama	4,089	79.3	47	North Dakota	635	99.4
23	Arizona	3,750	80.8	48	Alaska	570	99.6
24	Kentucky	3,713	82.3	49	Vermont	567	99.8
25	South Carolina	3,560	83.7	50	Wyoming	460	100.0

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The cumulative percentage column provides an easy way to see population concentration -- a reminder that generalization about numbers of states aren't always equivalent to conclusions about the number of people affected. In the extreme case, half the states could adopt a particular policy or experience a particular problem and only impact 15% of the population. Nine states have 52% of the population while 20 states have 76%.

Population Growth

American population grew by 1.4% between the April 1990 Census and the July 1991 estimate. This 15 month measurement, which moves the estimating date to the July date used by the Census Bureau between Census years, is equivalent to an annual rate of change of 1.11%. That growth is slightly above the annual rates reported in the 1980s. The 15-month changes for the states are shown in Table 2.

Table 2: Population Growth Percentage, April 1990 to July 1991

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Nevada	6.82%	18	North Carolina	1.63%	34	Michigan	0.79%
2	Alaska	3.64	19	Virginia	1.60	35	Kentucky	0.76
3	Idaho	3.18	20	Tennessee	1.56	36	Louisiana	0.76
4	Washington	3.10		**United States**	**1.39**	37	Mississippi	0.74
5	Oregon	2.81	21	Wyoming	1.32	38	Vermont	0.71
6	Utah	2.73	22	Minnesota	1.30	39	Kansas	0.69
7	Florida	2.62	23	Wisconsin	1.29	40	Pennsylvania	0.66
8	Colorado	2.52	24	Indiana	1.19	41	Iowa	0.65
9	Hawaii	2.44	25	Alabama	1.19	42	Maine	0.57
10	Arizona	2.32	26	Montana	1.13	43	West Virginia	0.45
11	Georgia	2.24	27	South Dakota	1.01	44	New Jersey	0.39
12	New Mexico	2.18	28	Illinois	0.98	45	New York	0.38
13	Texas	2.13	29	Nebraska	0.95	46	Connecticut	0.12
14	Delaware	2.10	30	Oklahoma	0.92	47	Rhode Island	0.10
15	South Carolina	2.09	31	Arkansas	0.89	48	Massachusetts	-0.33
16	California	2.08	32	Ohio	0.85	49	New Hampshire	-0.36
17	Maryland	1.65	33	Missouri	0.80	50	North Dakota	-0.63

The estimates show substantial disparities among the states. Nevada has been growing at a rate that would double its population roughly every 15 years. Four Northwestern states -- Alaska, Idaho, Oregon, and Washington -- are growing at twice the national average rate. Meanwhile, North Dakota and two New England states lost population.

State rankings in population growth closely resemble those in the Index of State Economic Momentum™ (Issue 24) and economic indicators such as employment, housing starts, and personal income. People tend to move toward economic opportunities and away from recessionary conditions.

This is vividly indicated by contrasting annual rates of growth of four states. In the first half of the 1980s, when the Midwest was suffering from recession, Illinois grew hardly at all (0.04% annual rate) while Colorado, Oklahoma, and New Hampshire were growing at 1.5% or better. In the late 1980s, when the Western states suffered from resource gluts, particularly in oil, Oklahoma lost 0.8% of its population every year and Colorado growth dropped to 0.55% while Illinois continued with no change, and New Hampshire boomed (2.25%) along with the rest of New England. From 1990 to 1991, Colorado grew at a 2% rate, Illinois and Oklahoma were just off the national pace with growth of about 0.75%, and New Hampshire lost a third of a percent of its population.

Sources Of Population Change

Population Change, 1990-1991
Rates Per 10,000 People

Source		Number
Natural Increase		81
Births	166	
Deaths	85	
Migration		30
From Abroad	30	
Within U.S. net	0	
Total		111

Population change is a result of two separate factors. The first is the *natural increase*, which is the additions to population from births and the subtractions from deaths. The second is *net migration*, which is the number of in-migrants minus the number of out-migrants. Table 3, at the left, shows the annual rates of change from the latest population estimates.

Without migration, U.S. population would grow annually by 81 people for every 10,000 people, or a growth rate of 0.81%. Migration from abroad adds 30 more people. Migration within the U.S. is a zero sum game for the nation, but not for individual states.

Natural Population Growth

Most states come close to having the national average increase in population of 0.8% a year from the surplus of births over deaths. As a result, without major migration, they could expect a gradual increase in demand for population-driven public services like transportation, education, and law enforcement.

Some of the states differ significantly from national patterns. The differences have major implications for state policies. States with high rates of natural population growth, like California and Hawaii, tend to worry extensively about such issues as quality of life and the environment, congestion, and regulation of growth. They need to spend more for infrastructure such as schools and roads.

Table 4 shows the leading and lagging ten states in birth rates, death rates, and the resulting natural increase in population. The first column shows the highest and lowest states in natural increases. Absent any new migration, Alaska's population would grow at 1.7% a year and Utah's at 1.56%. West Virginia, at 0.15%, would need a decade to show as much growth as these states would have in a year.

Table 4: Top And Bottom States In Natural Increase Factors
Number Per 10,000 Population, 1990-1991

Rank	Natural Increase		Births		Deaths	
1	Alaska	173	Alaska	211	West Virginia	106
2	Utah	156	Utah	208	Arkansas	104
3	California	132	California	204	Florida	102
4	Hawaii	122	Arizona	186	Pennsylvania	101
5	Texas	111	Texas	184	Missouri	98
6	New Mexico	110	Hawaii	182	Mississippi	97
7	Arizona	109	New Mexico	179	Alabama	97
8	Nevada	99	Nevada	172	Rhode Island	97
9	Colorado	96	Georgia	172	Oklahoma	96
10	Georgia	93	Louisiana	170	Iowa	96
	United States	**81**	**United States**	**166**	**United States**	**85**
41	North Dakota	56	Wisconsin	148	Texas	73
42	Oklahoma	55	Vermont	147	Nevada	73
43	Kentucky	52	Rhode Island	147	California	72
44	Maine	52	Kentucky	146	Idaho	72
45	Arkansas	50	North Dakota	145	New Mexico	69
46	Rhode Island	50	Montana	144	Wyoming	69
47	Florida	49	Pennsylvania	144	Colorado	64
48	Iowa	45	Maine	141	Hawaii	60
49	Pennsylvania	43	Iowa	141	Utah	52
50	West Virginia	15	West Virginia	121	Alaska	38

Because natural increase is births minus deaths, the way to have a high increase is to have a high birth rate and a low death rate. The second column shows the birth rates. They differ considerably although fertility rates (shown elsewhere in this issue) exhibit little difference. The percentage of the population that is women of childbearing age is more significant than how often those women have children.

The third column shows death rates. In the top four states, one out of every 100 residents will die before a year passes. In Utah, only about one in 200 will die in a year.

One key links the three columns: the age of the population. Western states have a younger population and thus a population more likely to have children and less likely to die.

The Impact of Migration

For the nation as whole, migration is less important to population growth than natural increases. This is not true for the individual states. The most rapid growth from 1990 to 1991 by natural increase was 1.7% in Alaska while the most rapid growth from migration was 4.3% in Nevada. The slowest natural growth was +0.15% in West Virginia, but 14 states lost population due to migration. The migration changes are shown in Table 5.

Table 5: Net Population Change From Migration, 1990-1991
Number Per 10,000 Population, 1990-1991

Rank	State	Number	Rank	State	Number	Rank	State	Number
1	Nevada	429	18	Virginia	46	34	Iowa	8
2	Idaho	166	19	Wisconsin	42	35	Missouri	7
3	Oregon	159	20	Maryland	41	36	Ohio	5
4	Washington	159	21	Alabama	36	37	Illinois	-3
5	Florida	158	22	Montana	34	38	Maine	-8
6	Alaska	118	23	California	33	39	Vermont	-11
7	Colorado	101		**United States**	**30**	40	Kansas	-13
8	Delaware	84	24	Indiana	29	41	Michigan	-14
9	Georgia	83	25	Minnesota	28	42	Mississippi	-14
10	South Carolina	83	26	Arkansas	22	43	Louisiana	-23
11	Arizona	73	27	Wyoming	21	44	New Jersey	-38
12	Hawaii	66	28	Oklahoma	19	45	New York	-43
13	Tennessee	64	29	West Virginia	19	46	Rhode Island	-44
14	Utah	62	30	South Dakota	16	47	Connecticut	-59
15	New Mexico	61	31	Nebraska	11	48	Massachusetts	-95
16	North Carolina	59	32	Pennsylvania	11	49	North Dakota	-109
17	Texas	57	33	Kentucky	9	50	New Hampshire	-118

The migration shown is "net." That is, migration of one person out of a state and one person into a state would have no effect on the numbers as the movement would have no impact on population change in either state.

Seven states gained population at an annual rate of more than 1%. All are Western states except Florida. Fourteen states lost population due to net migration. The movement exceeded 1% of population only in North Dakota, reflecting a pattern of decades, and New Hampshire, reflecting depressed economic conditions in New England.

Is it desirable for a state to be at the top of Table 5? Not everyone would answer the same way. Answering the question, and thus evaluating state performance, depends on where the in-migrants come from, why they came, and why out-migrants left. Assessing this is aided by the breakdowns of migration patterns in Tables 6 and 7.

Migration From Abroad

Table 6 deals only with migration from abroad. The net inflow, which adds 0.3% to population each year, is about the same as total immigration from abroad. There is almost no migration out of the United States.

Table 6: Net Population Change From Migration From Other Countries
Number Per 10,000 Population, 1990-1991

Rank	State	Number	Rank	State	Number	Rank	State	Number
1	Hawaii	87	17	Virginia	20	34	Georgia	8
2	California	83	18	Arizona	19	35	Indiana	8
3	New York	66	19	Utah	17	36	Missouri	8
4	Illinois	40	20	Alaska	16	37	North Dakota	7
5	New Jersey	40	21	Michigan	15	38	Montana	6
	United States	**30**	22	Oklahoma	15	39	New Hampshire	6
6	Texas	35	23	Kansas	14	40	North Carolina	6
7	Florida	32	24	Louisiana	14	41	South Carolina	6
8	Connecticut	25	25	Minnesota	14	42	Tennessee	6
9	Massachusetts	25	26	Idaho	12	43	Vermont	6
10	Washington	25	27	Pennsylvania	12	44	Alabama	5
11	Nevada	24	28	Delaware	11	45	Arkansas	5
12	Rhode Island	24	29	Iowa	10	46	Kentucky	5
13	Maryland	23	30	Wyoming	10	47	Maine	5
14	Colorado	20	31	Nebraska	9	48	Mississippi	5
15	New Mexico	20	32	Ohio	9	49	West Virginia	5
16	Oregon	20	33	Wisconsin	9	50	South Dakota	4

Table 6 is striking for the concentration of immigration. Forty-five states were below the national average. Thirty-seven states were two-thirds of the national average or less. Twenty states had less than 0.1% annual population growth from immigration, less than one third of the national average.

Immigration to California and New York and, to a lesser degree, the Chicago area and Northern New Jersey creates substantial demands on social services. Officials of these states see this immigration as creating major fiscal problems both at the state level and in communities like Chicago, Los Angeles, and New York. About the only thing on which California legislative leaders and the governor agreed upon in their late 1991 budget negotiations was that immigration burdens were one cause of the budget gap. They decided to press for federal policy changes so that more of the costs of services for migrants (e.g., welfare, Medicaid, schools) would be covered by the federal government. New York State and City officials have long held the same view. Table 6 suggests the problem they face. What they see as a major problem doesn't have much effect in most states.

Migration Within The United States

The rapid movement of people within the country shown by Table 7 is a tribute to how rapidly the American economy adjusts to change. It is also an indication of challenges faced by the states most affected.

In a single year, six states grew by more than 1% just from migration from other states. Nevada grew an astounding 4%. In the same year, four states saw more than 1% of their population pick up and leave.

Table 7: Net Population Change From Migration Within The United States
Number Per 10,000 Population, 1990-1991

Rank	State	Number	Rank	State	Number	Rank	State	Number
1	Nevada	405	18	Montana	28	34	Ohio	-4
2	Idaho	154	19	Virginia	26	35	Maine	-13
3	Oregon	139	20	Texas	22	36	Vermont	-17
4	Washington	134	21	Indiana	21	37	Mississippi	-19
5	Florida	126	22	Maryland	18	38	Hawaii	-21
6	Alaska	102	23	Arkansas	17	39	Kansas	-27
7	Colorado	81	24	Minnesota	14	40	Michigan	-29
8	South Carolina	77	25	West Virginia	14	41	Louisiana	-37
9	Georgia	75	26	South Dakota	12	42	Illinois	-43
10	Delaware	73	27	Wyoming	11	43	California	-50
11	Tennessee	58	28	Kentucky	4	44	Rhode Island	-68
12	Arizona	54	29	Oklahoma	4	45	New Jersey	-78
13	North Carolina	53	30	Nebraska	2	46	Connecticut	-84
14	Utah	45		**United States**	0	47	New York	-109
15	New Mexico	41	31	Missouri	-1	48	North Dakota	-116
16	Wisconsin	33	32	Pennsylvania	-1	49	Massachusetts	-120
17	Alabama	31	33	Iowa	-2	50	New Hampshire	-124

Substantial out-migration is a bad sign for a state from an economic development perspective. It means that people are voting with their feet -- working age people in search of better jobs and retirees in search of a better environment. Some of the movement is dramatic and publicized, such as California families seeking original California values by moving to Oregon and retirees from the Northeast moving to Florida and Nevada. But most migration isn't dramatic pulling up of stakes. Instead, it occurs when people leave for college, a temporary job, or military service and simply don't come back.

Substantial net in-migration is a sign that a state is doing something right. In economic development terms, it means that job or retirement opportunities are drawing new residents while few current residents are leaving.

THE FISCAL OUTLOOK

Introduction

With no sign that the economy has hit bottom, state finances continue to deteriorate. Most budgets for this year (FY 1992) are in worse shape than when enacted. Balances to begin the year and tax collections have both been below predictions. Spending -- particularly for Medicaid, AFDC, and corrections -- is above estimates in at least 35 states.

Because of structural deficits (Issue 1), the situation for some states would be grim even if economic growth were normal. Continued recession means slow revenue growth and continued recession-related spending. This year's solutions become next year's problems -- low balances, depleted rainy day funds, overdue bills, debt to pay back, and one-time devices that must be replaced with real revenues or spending cuts the next year.

Shortfalls And Their Cures

Table 8: Revenue Shortfall

1	Maryland	8.5%
1	Montana	8.5
3	N. Hampshire	8.4
4	Maine	6.7
5	Florida	5.6
6	Georgia	5.1
7	Rhode Island	4.4
8	Arkansas	4.3
9	California	4.1
9	S. Carolina	4.1
11	Washington	4.0
12	Virginia	3.7
13	Minnesota	3.5
14	Connecticut	3.4
14	Kentucky	3.4
16	Arizona	3.0
16	Nevada	3.0
18	Ohio	2.9
19	Michigan	2.3
20	Illinois	2.0
20	Tennessee	2.0
22	New York	1.7
23	New Jersey	1.6
24	Mississippi	0.7
25	New Mexico	0.6
26	Indiana	0.5

A recent NCSL survey found FY 1992 tax collections falling below estimates in 26 states. This understates the total by the number of states which were holding the bad news for release with the governor's budget in January. The list, at the left, shows 16 states with a revenue deficiency of 3% or more. For states with a fiscal year ending in June, that would mean making up double that, or 6%, by spending cuts that became effective in January. The situation is even worse in New York, where the fiscal year ends in March.

Some states with large shortfalls -- Maryland, Maine, Florida, and Georgia -- brought legislatures into session late in 1991 to adopt spending cuts. They went beyond employment freezes and one-time measures to include mid-year reductions in school aid, local government aid, and funds for higher education. Other states --California, Connecticut, and New York -- failed to act despite recommendations from the governor. In some states -- Illinois and Ohio -- the governor didn't recommend action before January. A few states are handling shortfalls without major cutbacks. Indiana came into the fiscal year better cushioned for downturns than most states. New Hampshire is one of the states taking advantage of Medicaid bootstrap financing now that its legitimacy is established. Its late 1991 legislative action is providing the salvation for the FY 1992 and probably the FY 1993 fiscal situation.

Possible Tax Increases

Money magazine's January issue guesses which states will raise taxes this year by giving each state grades: 21 "A" grades for no major change, 6 "B" for moderate chance of increase, 12 "C" for strong probability of increase, and 11 "D" for tax increases as a "sure bet." Table 9 shows the states classified as having some probability of enacting major tax increases in 1992.

Table 9: States Assessed By Money As Possibly Raising Taxes In 1992

Increase "Sure Bet"	Strong Probability	Moderate Chance
Florida*	Tennessee*	Texas
New Hampshire	North Dakota	Wisconsin
Illinois*	Mississippi*	New Mexico
Indiana	Alabama*	West Virginia
Kansas*	South Carolina	Arizona
Colorado*	Michigan*	California
Georgia	Montana*	
Ohio*	Virginia	
Rhode Island	Nebraska	
Maryland	Massachusetts	
New York*	Oregon	
	Louisiana	

Reports is aware of only one other published speculation on which of the 50 states will raise taxes, the **TaxWatch** list which appeared in State Budget & Tax News in its November 11, 1991 issue. An asterisk (*) in the table above indicates the states on that list.

The number of states on either the SB&TN or the Money list exceeds by a wide margin the number of states where governors and/or legislative leaders have indicated a tax increase is needed. This gap can be expected to narrow as time passes.

For example, when New York officials started talking about a shortfall last fall, legislative leaders and the governor agreed that a tax increase isn't the answer, that the answer lies in cutting spending. That was the easy part. Then they started discussing which spending to cut, how, and when. That proved to be the hard part. With no agreement through ten months of the fiscal year, Moody's reduced the state's already low bond rating. Standard and Poor's suggested a reduced rating was possible. While New York may not raise taxes, that alternative is more attractive in January than it was in October.

Doing What The Public Wants

> *It is not unusual for the public to want it both ways. They do not have to make the decision. But no matter what happens, it is likely to be unpopular and not be very well received.*

This quote could be from anyone looking at the choice between raising state taxes and cutting spending. It is from the managing editor of the California Poll, reporting on a November survey for the Sacramento Bee (12/20).

Those surveyed were given 16 categories of spending and asked if they would favor cuts. Cuts in 15 categories drew less than 25% support. In the 16th category 38% favored cuts but 44% favored spending about the same level. That category, regulation of business and the professions, involves minor outlays compared with the other categories. More than half the state's citizens want higher spending for mental health, the elderly and disabled, health care for the poor, law enforcement, public schools (highest with 65%), AIDS research, and aid to the homeless.

Three-fourths believe the level of state and local taxes is too high -- 38% say "much too high" and 38% say "somewhat high." Perception that taxes are too high is up from 59% in February. The increase probably results from tax hikes in the interim and the widespread publicity surrounding the legislative discussion of those increases before their enactment.

The clear and continuing preference of voters in California and elsewhere is that states increase spending and reduce taxes.

The Higher Education Perspective

> *As bad as the financial picture has been for higher education in this academic year, 1992-93 could be even worse.*

This was the Chronicle Of Higher Education's summary of its 50-state survey of higher education officials which appeared in its January 8 issue. Despite a grim outlook, higher education officials haven't been reluctant to ask for money. In over half the states, their budget requests call for increases above 10%. The second sentence of the magazine's summary concluded for higher education what **Reports** has concluded for all education, social services, health, and other state activities.

> *With many state legislatures beginning their 1992 legislative sessions this month, the recession and continuing budget rises in the states are expected to preoccupy lawmakers and overwhelm all the other issues affecting higher education.*

Will Fiscal Issues Be Tougher This Year? The Impact of Deferrals

FY 1993
The chickens come home
to roost

This graphic was part of the presentation the Rhode Island budget office made to executive and legislative leaders late last year. The detailed presentation explained the sources of the structural budget deficit and the compounding of that problem by the recession. On top of both structural and cyclical problems, in the new budget year (FY 1993), Rhode Island officials will have to deal with whatever problems they created by prior year actions. Rhode Island used "deferrals" in prior years that account for nearly 10% of the budget. The chickens coming home to roost include delays in school aid payments, rescheduling of debt service, deferral of certain employee compensation, and missing some scheduled employer contributions to retirement plans.

In California, the legislative fiscal office (Legislative Analyst) described a similar situation and warned that the FY 1993 budget would need "additional ongoing solutions," a polite way to describe permanent tax increases and spending cuts.

> *In acting on the 1991-92 budget, the Legislature made many very difficult decisions. Many of these decisions were targeted at resolving the structural portion of the budget problem. However, the expectation of an imminent economic recovery led the Legislature to also rely on short-term strategies to maintain programs until economic growth caused revenues to catch up. The failure of the recovery to materialize undermined these strategies, and leads us to the conclusion that the 1992-93 budget will require additional ongoing solutions.*

Not all states relied on deferrals to FY 1993 to solve their FY 1991 and FY 1992 budget problems, but many did. Not all of them will have to face the music in FY 1993, but many will.

Will Fiscal Issues Be Tougher This Year? Patience Wearing Thin

> *As I said last year and the year before that, this will only hurt for a little while although our projections suggest the situation won't improve.*

While the quote above is fabricated, it is how the fiscal message must sound to educators, health care providers, and others who have been affected by measures to deal with temporary adversity in state finances.

Clashing Claims: Every year there are issues pitting claimants for the states' resources against other claimants, indirectly against the taxpayer, and directly against the guardians of the resources like governors, legislative leaders, appropriations committees, and executive and legislative budget staffs. This year's major claims aren't new: (1) school aid and teacher salaries, (2) state employee compensation, (3) aid to local government, (4) reimbursement rates for health care providers, (5) welfare cash payments, (6) support of higher education, and (7) support of other state functions from the arts and corrections to zoos. Because, in this tight budget year, many claimants will get much less than they want, clashes will likely be sharp.

Clashes could be even sharper than the fiscal situation alone might suggest. The reason is that the outcomes will seem less temporary. It is one thing for a group like employees or nursing homes to accept less for one year when: (1) there are external causes like recession which are easily understood, (2) other groups seem to be suffering about equally, and (3) state officials can creditably make the case that the sacrifice is temporary and the group's long term aspirations will be supported in the long run. This story has led to widespread acquiescence in budget cuts in some circumstances. Although there were lively local controversies, from a national perspective this was the situation last year in California, Florida, Virginia, and some other states.

Permanent Temporary Problems: The "temporary" story wears thin when the temporary situation continues for a long time. This is increasingly the case in New England, as indicated by the ferocity of the battle over employee compensation measures in the Massachusetts legislature in November and December. It is also the case in states that have held the line on taxes for some years despite strong demographic pressures for increases, as typified by education budgets in Mississippi and Alabama.

The "temporary" story also wears thin where state officials talk simultaneously about structural budget deficits and a determination not to raise taxes. Examples are California and New York. Finally, some of the more raucous money disputes this year are likely in states that have escaped many of the effects of recession. There state officials can't easily blame economic necessity for what some groups see as parsimony. Look for major disputes, probably including teacher strikes, in Utah and Washington.

The spending-oriented groups often recognize that they aren't likely to achieve their objectives in a zero-sum competition with each other. So they coalesce to varying degrees around the concept of raising taxes. This worked in Missouri, which now faces choices more difficult than those of most states. Last year legislators and the governor agreed on a tax increase package that, under the state constitution, required voter approval. Voters rejected the package by a 2-1 margin in November. Now there are three bad choices: (1) try again with the voters, (2) adopt a smaller tax increase not requiring voter approval but risking voter wrath, or (3) live with existing resources.

STATES AND THE RECESSION

Introduction

Congress is now considering a variety of economic stimulus packages including tax cuts (see Issue 24 for impacts on states), aid to business, and new or expanded aid to state and local government. Federal grants of unrestricted cash and/or funds for public works were a common element of recession-fighting strategies in the 1960s and 1970s. These programs weren't repeated in the early 1980s recessions, in part because the earlier programs had clearly had their major spending impacts well after the recessions had ended.

Stimulating The Economy -- The Gang That Couldn't Shoot Straight

Many state and local officials have counseled that altering matching requirements in grant programs would be a simple and fast way to use state and local government to inject added spending into the economy and/or to prevent tax increases that would otherwise take place. The Congress reflected this approach (and concerns about the ability and willingness of state and local officials to provide matching money) in two small grant programs last year -- drug control and the new housing (HOME) program.

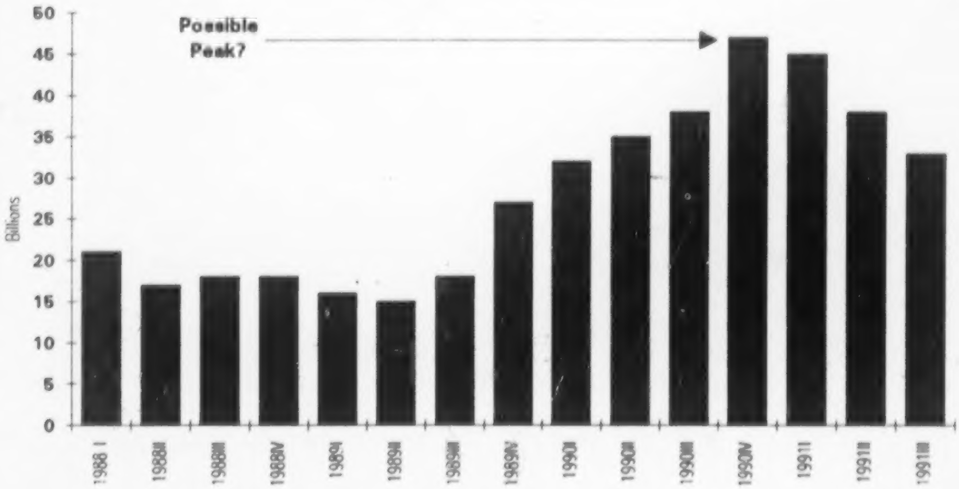
The surface transportation bill was the major Congressional action affecting matching. It permits states to spend without match and pay their match later, in effect borrowing their match. The bill was highly touted by the President and Congressional leaders as a job-creating bill. The first problem was that the legislation passed after the old law had expired, adding delay to the already existing uncertainty about what the new rules would be. The second problem was that the new law, in the words of Federal Funds Information for States, "inadvertently reduced the 1992 federal-aid highway obligation ceiling by $1.2 billion."

How, one might ask, can Congress -- with a budget of over a billion dollars for the sole purpose of making good policy decisions -- possibly *inadvertently* knock $1.2 billion out of highway and transit spending while trying to make a record of accelerating public works? The answer is, not surprisingly, complex. Part of the problem comes from a decision to convert an old post office in Brooklyn into a courthouse in 1994. Under the budget control legislation, this decision works its way back into FY 1992. In FY 1992, it affects the highway obligation limit. Those involved in the Congress will seek corrective legislation early this year, but FFIS expects that legislation to correct only $1 billion of the $1.2 billion error and notes "even passage of this legislation will delay the availability of highway obligational authority to the states."

Stimulating The Economy, Perverse State and Local Officials?

The Joint Economic Committee has already started hearings on policies to deal with recession. Witnesses are suggesting ways for government to add to purchasing power by taxing less or spending more, increasing deficits in the process. This is the traditional Keynesian prescription for recession fighting. State and local officials march to the beat of a different drum: requirements for balanced budgets. By constitutions, statutes, and campaign promises, they are encouraged not to overspend their revenues. As a result, their economy-stimulating deficits in recession are the accidental results of underestimating spending and overestimating revenues. The result is deficit spending. It shows clearly in the chart below as rapid growth in state and local deficits in 1990.

State And Local Deficits By Quarter



The chart, drawn from Commerce Department data, shows that decisions in 80,000 state and local governments are having their expected impact. Taxes are being raised and spending is being cut to restore balanced budgets. Deficits are trending downward, which is the wrong result from the perspective of those looking for economic stimulus.

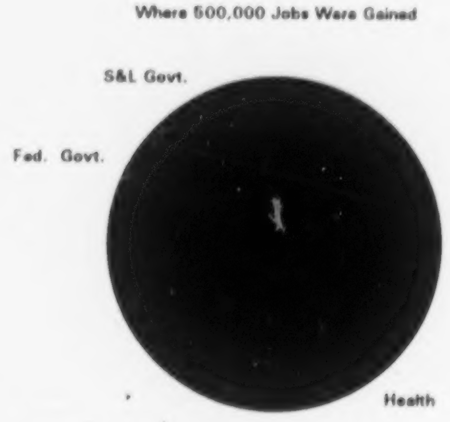
The state and local deficit won't drop below a $15-25 billion annual rate primarily because of continuing bond-financed capital outlays. Inflation and a growing population mean these governments are constantly borrowing more than they repay. Using debt-financed capital is the major way state officials can simultaneously act to stimulate their economies and comply with their balanced budget requirements.

Look for a boom in these proposals this year, already signaled by their prominence in the state-of-the-state messages of the governors of California, New Jersey, and New York. Debt-financed capital outlays will grow for another reason. States in the South and West that have traditionally relied on pay-as-you-go financing are increasingly turning to borrowing, which relieves pressures on their regular budgets. For example, pay-as-you-go capital was sharply curtailed in Virginia's budget cutbacks in 1990 and 1991. Now the governor proposes financing higher education projects by borrowing.

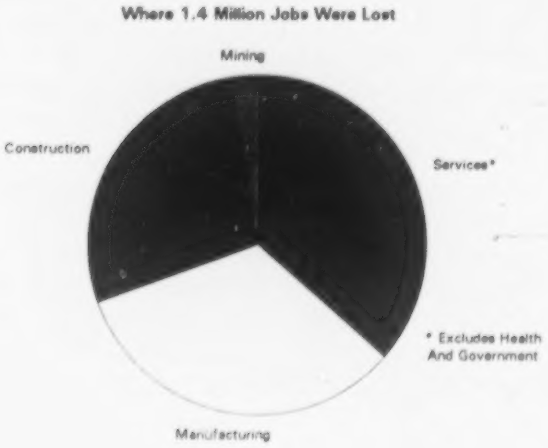
Where Jobs Are Lost And Gained

While by no means immune from the impacts of economic downturn, governments tend to be a stabilizing force in recession. This pattern is appearing in the current recession. While the economy lost 888,000 jobs between November of 1990 and November of 1991, government employment grew by 97,000 jobs. This 0.5% increase wasn't large enough to match population growth of about 1%, but tended to offset some of the much larger loss of jobs in the private sector.

The small gain in government employment was part of a larger gain in service jobs, but these failed to offset even larger losses in goods-producing jobs. Overall in the year ending in November, there were gains of about 500,000 jobs in some industries and losses of 1.4 million in others.



As shown in the chart, the bulk of the 500,000 job gain was in health care. The 403,000 new health jobs represented an increase of 5% in a single year. Government accounted for the rest of the gain. With revenues most adversely affected by business conditions, states cut employment about 21,000. Local employment increased 97,000. The state decrease was 0.5% while the local increase was about the same percentage and the federal increase was 0.8%.



The profile of the 1.4 million jobs lost, shown at the left, reflects the concentration of losses in the goods-producing sectors of the economy. In a single year, 5.3% of mining jobs disappeared. So did 7.6% of the nation's construction jobs and 2.4% of manufacturing jobs. Within manufacturing, losses were 3.7% in making durable goods like cars and appliances and only 0.7% in making non-durable goods such as food products and apparel.

For those who worry about the competitiveness of the U.S. economy, these statistics are likely to be alarming. Most of the job losses occurred in sectors that produce outputs that can compete with other nation's. All the job gains occurred in activities that are essentially consumptive, producing nothing to be traded with other nations or to raise future national output.

This distinction can be taken too far. Some services, such as health care, are sold to foreign nationals. There is no reason to call a municipal electric worker in Los Angeles non-productive because he works for government while calling one in Boston productive because he works for a private electric company. Also, some spending on health care and education arguably contributes to production. But most of the expansion in state and local employment was probably related to corrections and social work. Most of the expansion in health care probably was associated with caring for persons who will not be working -- those over 65, the disabled, and the terminally ill.

Tax Policy

There isn't much on-the-record discussion of tax policy so far this year. Tax cuts of any significance are pretty much out of the question. As described in Issue 1, the states with the best economic performance have special demands limiting resources available for tax relief, while other states don't have the resources to consider the possibility.

Tax increases are still being treated as an unthinkable option in most states. Particularly in states with legislative elections this year, tax hikes are currently the off-the-record, under-the-table option for governors and legislative leaders.

But in many states, the leading tax options are clearly defined. In Minnesota and Wisconsin, they are options previously passed by the legislature and vetoed by the governor. In Missouri, they are a scaled down version of the package rejected by voters in November. In Kansas, they are a scaled down version of the sales tax increases proposed last year by the governor but not passed. In the Dakotas, they are the sales tax increases that have been considered and rejected over the past several years. In Massachusetts, the leading tax option is the sales tax increase long backed by education groups. In Illinois, it is the flat rate income tax increase that is beginning to be discussed.

Leading Tax Options

If raising taxes were like playing musical chairs, what options would lawmakers select when the music stopped? Probably about the same kind of mixture that was adopted in 1991. It would include selections from a long list: (1) rate increases in the sales tax and more broadening of the base, (2) income tax rate increases in the higher brackets, perhaps with relief for low income taxpayers, and across-the-board rate increases, (3) increases in selective excise taxes such as alcohol and tobacco taxes, (4) increases in corporate income and franchise taxes, particularly when personal taxes are being increased, and (5) the major changes in health provider taxes necessary to come into line with federal rules on Medicaid bootstrap financing.

Increasing local taxes should again be popular, particularly in ways where state officials don't leave their footprints on local increases. Raising the local effort requirement in school aid programs will achieve this result, provide more money for education, and help satisfy those complaining and litigating over inequity in school finance. Offering additional local option taxes and broadening the purposes for which existing authority can be used should also prove popular.

Increasing state taxes to relieve local property taxes is always a popular concept. The topic is particularly hot in states under pressure from voters to reduce property taxes. In Idaho, where a ballot measure to limit taxes is under discussion, the governor has held a tax summit. In his state-of-the-state message, he endorsed trying to find a way to limit local property taxes. In Oregon, where a property tax limit measure has already passed and income taxes are high, most state leaders in and out of government quietly agree on the solution. But that solution, adopting a sales tax, has been rejected by voters every time it has been proposed.

In states not under pressure of voter initiatives, there will probably be considerable caution about raising state taxes to lower property taxes. If nothing else, the fate of New Jersey legislators backing such a measure may cause legislators in other states to wait until after the 1992 elections to make any such move.

Taxing Business

Three states -- Florida, New Hampshire, and maybe Louisiana -- offer the greatest possibilities for innovations in business tax policy. All three states need money to maintain current services, though current thinking in New Hampshire is that Medicaid bootstrap financing adopted in a special session late last year may have solved most of the immediate problem. Officials of all three states have constraints against a major broad-based tax. Florida can't have a personal income tax without a voter-approved constitutional amendment that polls indicate voters won't support. Louisiana's property tax is constrained by a massive homestead exemption. Many New Hampshire officials, including the governor, have "taken the pledge" against adopting either a sales or personal income tax.

There are major constraints on raising the corporate income tax in all three states. Many Louisiana officials and business leaders are convinced that the state already relies too heavily on business taxes. Florida, and particularly New Hampshire, find that much economic activity gets organized in non-taxable proprietorships and partnerships rather than corporations. The profits tax rate is already high in all three relative to competitor states.

Governor Chiles vaguely describes a Florida solution as a "broad-based business tax." Consulting reports turn this concept into a value added tax similar to Michigan's. Past reform studies in Louisiana have also focused on the value added concept. New Hampshire has seen many proposals defining business activity plus a family of proposals that provide a corporate tax equivalent for income of proprietorships and partnerships.

Nevada faced problems similar to those of these three states, but acted in 1991 to cure them with what closely resembles a "head tax," a tax on the number of employees. The combination of dissatisfaction with this type of tax and a state budget that needs added revenue could cause business tax issues to be revisited.

HEALTH COSTS BEYOND MEDICAID

Don't look for any dramatic changes or roll call votes on massive revisions of health care financing this year. But do look for the subject to affect policymaking indirectly in spending, tax, and even in regulatory activity. These pervasive effects aren't always explicitly identified, but this doesn't make them less important, just less well understood.

How pervasive are the effects? Sometime, probably last year, the nation's health care bill passed the state and local tax bill in size. Put another way, Americans are paying more for health than for all state and local activities put together.

While Medicaid cost increases get most of the attention, rising health costs in other areas of state budgets are part of the continuing cost pressures causing tight budgets, spending cutbacks, and tax increases.

Employee Health Care: Health care for state employees is one major category. Generally states pay all or nearly all health insurance costs for employees and retired employees. Many states pay most or all the costs of coverage for their dependents. Higher prices and increased use of services have tended to produce double-digit increases in cost per person covered by employee health insurance just as they have for Medicaid. Attempts to control these costs have proven equally ineffective. Most states have refrained from shifting the costs to employees, respecting a willingness of employee organizations to live with lower (taxable) salary increases to keep higher (non-taxable) benefits.

A few states have tried to handle fiscal problems by delaying payment of health bills for employees, as well as delaying payment of Medicaid bills. West Virginia did this in the late 1980s to the point that some doctors wouldn't serve state employees unless the employees themselves made the payment. That situation was reached with some physicians in Illinois last spring and apparently will arise again this spring. The shortfall in employee health insurance is about $100 million, part the delayed payment of bills carried over from last year and part unanticipated cost increases.

Health Care For Retirees: Many states cover the health care costs of retirees and, often, their dependents. For employees that have reached age 65, Medicare covers most, but not all, of the costs. For the many employees retiring before age 65, annual costs can run $5,000 per person. This liability has become large relative to the cash pension. As a result, those who control accounting practices have argued that they should be forward funded during the employees' working years, just as the cash pension is. Without any exceptions known to **Reports**, states aren't doing this. To comply with private accounting standards, more and more large companies are recognizing an actuarially determined amount each year as an expense and setting funds aside to pay health costs after retirement.

Among the private companies, coverage of retiree health costs is common among state-regulated companies that provide electric service, water supply, natural gas distribution, and local telephone service. The effect of current funding of these future health costs is to increase the operating costs of these utilities and, other things being equal, increase the rates states let them charge customers. Rate increases for this purpose have already been granted in Connecticut, Florida, North Carolina, and probably other states. But, at least temporarily, regulators in Georgia and Hawaii have rejected the increase requests. Cases are pending in most of the larger states. The increases involved are in the broad 1-5% range.

COMPARING STATE AND LOCAL TAX BURDENS

For the past several years, Money has compared state tax burdens using sales, income, and gasoline taxes. This predictably skewed the comparisons by showing light burdens in states with high local property taxes. In its January issue, the magazine has remedied that deficiency with some dramatic changes. For example, New Hampshire dropped from having the second lowest tax burden to the tenth. The new rankings are shown in Table 10.

Table 10: State And Local Taxes On Money Household, 1991

Rank	State	Tax Bill	Rank	State	Tax Bill	Rank	State	Tax Bill
1	New York	$8,841	18	Michigan	$6,635	35	Alabama	$5,343
2	Oregon	8,168	19	California	6,610	36	New Mexico	5,332
3	Maryland	7,986	20	New Jersey	6,597	37	Mississippi	5,185
4	Massachusetts	7,830	21	North Carolina	6,507	38	Missouri	5,185
5	Wisconsin	7,762	22	South Carolina	6,480	39	Delaware	4,753
6	Rhode Island	7,716	23	Georgia	6,417	40	North Dakota	4,530
7	Maine	7,673	24	Colorado	6,269	41	New Hampshire	4,299
8	Minnesota	7,145	25	Connecticut	6,201	42	Louisiana	4,254
9	Utah	7,121	26	Kansas	6,144	43	Washington	3,845
10	Nebraska	7,052	27	Indiana	6,084	44	Texas	3,625
11	Iowa	7,016	28	Arizona	5,892	45	South Dakota	3,470
12	Virginia	6,868	29	Kentucky	5,871	46	Tennessee	3,354
13	Idaho	6,863	30	Illinois	5,830	47	Florida	3,185
14	Ohio	6,849	31	Oklahoma	5,684	48	Wyoming	2,717
15	Montana	6,700	32	Pennsylvania	5,676	49	Nevada	2,588
16	Hawaii	6,693	33	Arkansas	5,585	50	Alaska	2,013
17	Vermont	6,643	34	West Virginia	5,374			

The typical household used for comparisons was definitely a higher income household, one the magazine says is typical of its subscribers. Adjusted gross income in a four person household is nearly $75,000. The high income used for comparison and the exclusion of hidden taxes (e.g., franchise, corporate income, gross receipts) mean that the comparisons have limitations. However, using relatively high incomes and ignoring hidden taxes are probably appropriate for people that might consider moving for tax purposes.

The magazine quotes a Gallup Poll indicating 6% of Money subscribers interviewed had moved to another state to save on taxes, up from 3% who said they had moved for this purpose in 1989 and 1990 polls. Some 22% said they had considered changing states to save on taxes. This isn't representative of the national population, however, as Money subscribers are disproportionately retired or nearing retirement age, have more money than most, and, as indicated by their subscription, worry about finances more.

FERTILITY AND BIRTH RATES

The birth rates relevant for calculating changes in population relate population created by birth to the population that already resides in a state, regardless of age. While this is the right concept for explaining population growth as is done in the lead article in this issue, it says nothing about the propensity to bear children. Clearly a state like Florida with lots of persons over 65 will, other things being equal, have fewer births per resident than Western states with a younger population.

The fertility rate, shown in Table 11, focuses on those who have babies -- females between ages 15 and 44. In any given year, 0.7% of these women, or 692 out of 10,000, have a child.

Table 11: Births Per 10,000 Females Aged 15-44, 1969

Rank	State	Number	Rank	State	Number	Rank	State	Number
1	Utah	898	17	Kansas	681	34	Montana	638
2	Alaska	897	17	Maryland	681	34	North Dakota	638
3	Arizona	834	19	New Jersey	674	34	Wisconsin	638
4	California	822	19	South Carolina	674	37	Massachusetts	635
5	New Mexico	764	21	Arkansas	669	38	Oklahoma	633
6	Texas	753	22	Michigan	668	39	Colorado	631
7	Nevada	743	23	Delaware	662	40	Indiana	630
8	Hawaii	742	24	Nebraska	660	41	Rhode Island	628
9	Florida	723	25	Connecticut	659	42	Tennessee	623
10	Mississippi	706	25	Minnesota	659	43	Pennsylvania	617
10	South Dakota	706	27	Missouri	657	44	Oregon	610
12	Georgia	700	28	New Hampshire	655	45	Maine	609
13	Illinois	692	28	Washington	655	46	Iowa	608
13	Louisiana	692	30	North Carolina	650	47	Kentucky	605
	United States	**692**	31	Virginia	645	48	Vermont	598
15	New York	690	32	Ohio	644	49	Wyoming	585
16	Idaho	682	33	Alabama	642	50	West Virginia	515

The differences among states are relatively slight. While West Virginia is 26% below the national average, no other state is more than 15% below it. Only five states are 10% or more above the national average. Small differences among states in the middle of the table are probably meaningless. Small errors in the estimate of female population can produce significant swings in the reported fertility rate. In general, Blacks, Hispanics, and members of the Church of Jesus Christ of The Later Day Saints (Mormons) have higher birth rates than other population groups.

INITIATIVE AND REFERENDUM

The deadline for putting voter initiated measures on the June California ballot passed with no measures qualified by the nearly 400,000 signatures needed. There were 13 measures on the November ballot. Initiated legislation and constitutional amendments have been a major force in shaping California policy and have had significant impacts in other states. Examples: Proposition 13 property tax limits, Proposition 98 guaranteeing education funding, Proposition 103 on insurance regulation, and Proposition 104 on legislative terms and staffing. There was considerable speculation that California's initiative process would prove nationally significant on other issues, such as health insurance.

Theories of what happened abound. Perhaps those interested in California politics are preoccupied with reapportionment. Perhaps those who finance campaigns are short of money because of recession. Another highly plausible theory is that potential sponsors and funders of initiative campaigns are afraid they can't win because of the tendency voters exhibited in the November election -- voting NO on every initiative.

MIGRATION OF WELFARE RECIPIENTS

In some states there is concern that welfare benefits well above those of other states are drawing welfare recipients. Such movement, if significant, would raise state costs for schools and welfare and increase concentrations of low income residents without any obvious benefits. The solution, being pushed particularly in California and Wisconsin, is capping benefits for new residents so they wouldn't gain by migration. Critics argue that there is no significant movement of recipients to higher benefit states.

Data has been scarce. Wisconsin's social service secretary offers some in an OpEd piece in the Milwaukee Journal (12/29). In a recent three month period, the state acquired information on residency of new AFDC recipients. Statewide, 12% had been in the state less than 90 days and never lived in Wisconsin before. In Milwaukee, the figure was 20%. An AFDC family of three gets $517 there, but only $367 in nearby Chicago. The Thompson Administration will again push for a four county demonstration program. For six months, new AFDC families would get only the benefit level of the state from which they came. The proposal lost by a narrow margin in the legislature last year.

Must a state treat all its residents equally? Under the "right to travel" in the U.S. Constitution and bills of rights in state constitutions, a case can be made that past residency can't be used in determining benefits. This was the conclusion when Alaska tried to pick long-time residents for special benefits paid from its oil money. But merely setting foot in a state and declaring an intent to stay isn't enough to get equal rights to every state service. If it were, there would be no one paying non-resident tuition at state universities.

STATISTICS ON RACE

Information involving race appears infrequently in state legislative debates and in Reports. One reason is that racial distinctions aren't generally relevant to the decisions to be made. For example, the concerns about persons migrating to get higher welfare benefits have been over persons of: (1) Race A when Washington worried about the problem in its general assistance program in the late 1980s, (2) Race B in Wisconsin (discussed above), and (3) Races B and C in California. Knowing which is which race isn't seen as aiding policymaking in situations like these, at least by most policymakers. The resulting policy will be color/race blind for legal reasons, if not policy reasons.

Another problem is that statistics based on race/ethnicity are seriously flawed conceptually and operationally.

Conceptually, there isn't symmetry in treatment of ethnic groups. Remember the WASP (White-Anglo-Saxon Protestant) that people used to rail against as having power and privilege? WASP was defined exclusively. So a child of a WASP and a non-WASP wasn't a WASP. Black was defined inclusively, so if either parent was black, the child was defined as black. The child's child was also black. As a result, no one talks about WASPs anymore because WASPs have intermarried with Catholics, Germanic groups, Asians, and blacks. In 1989, some federal definitions were changed. For example, a black child results from the union of a black mother and a white father, but reversing the races of the parents produces a white child.

All these definitional fine points are lost on citizens. This is important because in a national Census, a survey, or on intake forms in schools, social service programs and hospitals the practical definition of race/ethnicity is whatever box someone checks on a form. The results are assessed in three articles in the Journal Of The American Medical Association (1/8). Conclusion: "individuals may be assigned a different race at birth, during the course of life, and at death." One practical implication explored by the articles is that infant mortality statistics by race are flawed because some children are counted as black in the birth count but counted as white if they die within the first year of life.

POPULATION ESTIMATES IN POLITICS

Expect controversy over population estimates to continue for the next several years as representatives of states and cities most affected by possible undercounts seek to have their estimates increased. Getting an estimate increased can affect political power as measured by representation in legislatures, the Congress, and the electoral college that selects the President. Population also enters into the federal limits on certain tax-exempt bonds. In some programs, the amount of federal assistance is a function of population, so higher estimates would bring more federal money.